No. 10356

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

GUARANTY TRUST COMPANY, a corporation, as liquidating trustee of Yakima Holding Corporation,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

and

UNITED STATES OF AMERICA,

Appellant,

vs.

GUARANTY TRUST COMPANY, a corporation, as liquidating trustee of Yakima Holding Corporation,

Appellee.

BRIEF OF APPELLANT, GUARANTY TRUST COMPANY

UPON APPEALS FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE EASTERN DISTRICT OF WASHINGTON SOUTHERN DIVISION

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JURISDICTIONAL STATEMENT

This is an action against the United States to recover deficiency assessment of income tax and excess profits tax illegally imposed by the Commissioner of Internal Revenue and paid by plaintiff. The District Court had jurisdiction under the Tucker Act and the Internal Revenue Code. Title 28 U. S. C. A. sec. 41 (20) and Title 26 U. S. C. A. sec. 3772. It is undisputed that the Collector of Internal Revenue who received the payment was no longer in office at the time of commencement of the action. (Tr. 3, 14, 16, 17, 495)

The case also comes within the usual appellate jurisdiction of this Court upon appeal from final judgment of District Court in such tax cases. Title 28 U. S. C. A. sec. 225, 226, 765, 875.

STATEMENT OF THE CASE

This is an action brought by Guaranty Trust Company, a corporation, as liquidating trustee of Yakima Holding Corporation, a corporation, against the United States under the Tucker Act and the Internal Revenue Code to recover a refund of the sum of $26,933.86, together with interest and costs, the same having been paid to the government on May 27, 1938, pursuant to deficiency assessment made by the Commissioner of Internal Revenue as to the 1935 income tax and excess profits tax of said Yakima Holding Corporation.

The District Court entered judgment for plaintiff in the sum of $12,793.04, together with interest and costs. (Tr. 498) Each party has appealed, and we shall therefore designate them as plaintiff and defendant, respectively, as they appeared in the District Court. We shall also for brevity refer to Yakima Holding Corporation as the Holding Company and to Yakima First National Bank as the Bank.

The basic question is whether the profit realized in April 1935 from the sale of 11,000 shares of stock of Sunshine Mining Company was properly taxable to the Bank as contended by plaintiff or to the Holding Company as contended by defendant. The stock in question consists of two blocks, one consisting of 7500 shares purchased in August 1934, and sold in April 1935, and the second consisting of 5000 shares purchased from Alexander Miller in December 1934, of which 3500 shares were sold in April

1935, and the remaining 1500 shares were retained by the Bank until 1938. The Commissioner also levied, and plaintiff paid, a 50% fraud penalty.

The District Court after a non-jury trial held that the profit on the 7500 shares was taxable to the Holding Company, but that the profit on the sale of the 3500 Miller shares was properly taxable to the Bank and not to the Holding Company; and that plaintiff was therefore entitled to recover back the tax based on the profit from the sale of the 3500 shares and also the entire fraud penalty, which the court held was improperly assessed.

It is our contention that both the 7500 and the 5000 share blocks of Sunshine stock were held by the Holding Company in trust or as agent for the Bank, and that the profit on the sale thereof was therefore taxable to the Bank as the beneficial owner thereof and not to the Holding Company.

The facts are not substantially in dispute and may be summarized as follows:

During the years in question, 1934 and 1935, Yakima Holding Corporation was a holding corporation owning practically all of the stock of Yakima First National Bank, First National Bank of Wapato, and the majority of the stock of Guaranty Trust Company. Yakima First National Bank and Guaranty Trust Company had adjoining but entirely separate places of business in the city of Yakima. R. M. Hardy was President and Manager of said Bank and

President of the Holding Company. George H. Bradshaw was Secretary and Manager of Yakima Holding Corporation and Guaranty Trust Company. The only office of the Holding Company and Mr. Bradshaw was in the Guaranty Trust Company's place of business. (Tr. 5, 16, 91, 92, 115-118, 143, 155)

Several years previously during the depression, Yakima National Bank had taken over and merged with the First National Bank of Yakima to form the Yakima First National Bank. The First National Bank was in shaky condition and had numerous assets of doubtful value, which were severely criticized by the national bank examiners. At the time of the merger the bank examiners agreed with Mr. Hardy that he might have five years to work out the doubtful assets. Alexander Miller, a wealthy citizen of Yakima, was a large stockholder in the First National Bank and was naturally grateful to avoid a bank stockholders' assessment. Mr. Miller was also the Treasurer of Sunshine Mining Company and a stockholder in the Holding Company. (Tr. 97-101, 144)

The continuance and increased severity of the depression, however, made the working out of the doubtful assets extremely difficult. Although the agreed five year period had not expired, the national bank examiners repeatedly urged the Bank and Mr. Hardy, its President, to obtain $200,000 cash from the Reconstruction Finance Corporation through the issuance to it of preferred stock with the view

of improving the financial condition of the bank and avoiding impairment of its capital. The bank, however, although at one time making such application to the R. F. C., preferred to retain its independence and not to issue such preferred stock. (Tr. 97-100, 220, 246)

In August 1934 Mr. Hardy was also President of Sunshine Mining Company and negotiations were pending for the listing of its stock on the New York Curb Exchange and later the New York Stock Exchange. It was then apparent to Mr. Hardy and the other officers of the Bank that the market value of stock in Sunshine Mining Company was going to increase very substantially. This presented an obvious and effective method of improving the Bank's financial condition so that the doubtful assets could be charged off, the national bank examiners satisfied, and the necessity for issuing preferred stock to the R. F. C. avoided. However, it was apparent that the Bank could not directly purchase and pay for Sunshine Mining stock in its own name, in view of the limitation upon the statutory powers of national banks.

Accordingly, in August 1934 it was definitely orally agreed between the Bank and the Holding Company through their respective officers, directors, and executive committees that the Holding Company would purchase and pay for 7500 shares of Sunshine stock and was to hold the same in trust for and on behalf of said Bank and that the Bank and not the Holding Company was to be at all times the

sole beneficial owner and holder thereof; that at the time of the future sale of said stock the Bank was to pay the Holding Company the actual cost of said stock plus a reasonable "appreciation write-up" as compensation for its services and that in the meantime the Holding Company should receive and retain the dividends paid thereon as further compensation for its services; and that if any loss resulted from the purchase and sale of said stock the loss would be borne entirely and exclusively by the Bank and it would reimburse the Holding Company therefor; and that if any profit resulted therefrom, as it was believed was almost certain to occur, the entire profit therefrom, less the said "write-up" and dividends, would inure and accrue to and for the Bank and would be paid to it, and said profits would be the property of the Bank entirely and exclusively.

This agreement is shown by the uncontradicted evidence of Messrs. Hardy, Rightmire, and Crawford, three officers of the Bank. (Tr. 82-89, 93-97, 143, 156-159, 164-5, 170-1) Mr. Miller and Mr. Bradshaw died prior to the trial. (Tr. 40, 41)

In August 1934 pursuant to this oral agreement the Holding Company purchased 7500 shares of Sunshine stock and paid the purchase price thereof in the sum of $59,576.50. The Holding Company was then indebted to the Bank in the sum of $60,000, and at that time the Holding Company received $75,000 in cash from Mr. Hardy in payment of a loan which he owed the Holding Company. Stock certificates

for 2500 shares were issued in the name of George H. Bradshaw, the Secretary and Manager of the Holding Company, and also a director and member of the executive committee of the Bank, as a "street name", and certificates for the other *5000 shares were issued to and in the name of Yakima First National Bank.* (Pl. Ex. 1, 5; Tr. 25, 256, 267) All of these stock certificates were held in the possession of the Bank.

In the early part of December 1934 or prior thereto there were a number of conversations whereby it was agreed between Mr. Alex Miller, the Bank, and the Holding Company, that Miller would transfer and exchange to the Holding Company 5000 shares of Sunshine stock on the basis of $12.00 per share, for 4000 shares of Yakima Holding Corporation stock on the basis of $15.00 per share, to be transferred from the Holding Company to Miller; and that the Holding Company would receive said Sunshine stock wholly as trustee and agent for the Bank and that the entire transaction was solely and directly for the benefit of the Bank. As hereinabove stated, Mr. Miller was a large stockholder in First National Bank which had been merged into Yakima First National Bank, as well as a man of considerable wealth, and he was very desirous of assisting the Bank to rectify its impaired capital position. (Tr. 101-106, 120, 121, 144)

The testimony of Mr. Hardy is undisputed:

"Mr. Miller had originally on a number of occasions *offered to sell to the Bank* some Sunshine Mining stock

at a low price. I explained to Mr. Miller that the Bank couldn't buy it. This deal was finally worked out and handled thru the Holding Corporation.

Q For what purpose?

A *For the benefit of the Bank.*" (Tr. 144)

This transaction was further evidenced by the following three letters signed and delivered by said parties on December 11, 1934:

"Yakima Holding Corporation

December 11, 1934

"Mr. Alex Miller
Yakima, Washington.

Dear Sir:

"Referring to conversations which we have had recently regarding an exchange of some stock of the Yakima Holding Corporation for stock of the Sunshine Mining Company, I wish now to make the definite proposition that we will exchange four thousand shares of Yakima Holding Corporation stock for five thousand shares of Sunshine Mining Company stock. This is putting a value of $15.00 per share on the stock of the Holding Company and $12.00 per share on the stock of Sunshine.

Yours very truly,

GEO. H. BRADSHAW
Secretary

GHB:M

Ap. 25.35

Delivered Sunshine Cert. for
5000 shares to Mr. Hardy
GHB"

(Pl. Ex. 16, Tr. 312)

Mr. Miller on the same date replied thereto by letter reading as follows:

"December 11, 1934

"Mr. Geo. H. Bradshaw, Secretary,
Yakima Holding Corporation,
Yakima, Washington.

Dear Sir:

"Referring to your letter of this date, in which you offer to exchange four thousand shares of Yakima Holding Corporation stock for five thousand of Sunshine Mining stock, I wish to advise you of my acceptance of this offer of exchange.

Yours very truly,

ALEX MILLER"

(Pl. Ex. 17, Tr. 313)

On the same date Mr. Miller delivered to Guaranty Trust Company to hold in escrow certificate for five thousand shares of Sunshine stock, together with escrow letter reading as follows:

"December 11, 1934

"Guaranty Trust Company,
Yakima, Washington

Gentlemen:

"I am handing you herewith a certificate for five thousand shares of the stock of the Sunshine Mining Company, which I authorize you to deliver to the Yakima Holding Corporation in exchange for a certificate for four thousand shares of its capital stock.

"I wish, however, to make it a condition that this exchange will not be completed unless a sum sufficient to make the total of new money to be provided for the Yakima Holding Corporation equals a sum of at least $200,000.00, and to be completed by March 1, 1935.

Yours very truly,

ALEX MILLER"

(Pl. Ex. 18, Tr. 314)

It is undisputed that the condition imposed in the last paragraph of this letter was later waived by Mr. Miller. (Tr. 105, 106) The Holding Company did not have the 4000 shares of its stock readily available at that time and therefore the 5000 shares of Miller's Sunshine stock remained in escrow in the possession of Guaranty Trust Company until the same was sold in the latter part of April 1935 as hereinafter stated. (Tr. 147) In December 1934 the market value of the Holding Company stock was greatly less than $15.00 per share. (Tr. 124)

On the following day, December 12, 1934, the oral agreement with reference to the 7500 shares was confirmed in writing by the very important Plaintiff's Exhibit 19, (Tr. 47, 315) a letter written on that date by Mr. Bradshaw, Secretary and Manager of the Holding Company, to the Bank, reading as follows:

"Yakima Holding Corporation
Capital Paid in $1,400,000.00
R. M. Hardy, President
Alex Miller, Vice Pres.
Geo. H. Bradshaw, Secretary
A. E. Larson, Treasurer
Yakima, Washington

December 12, 1934

"Yakima First National Bank
Yakima, Washington

Gentlemen:

"*In order to confirm an understanding we have had with the bank regarding the purchase of 7500 shares*

of Sunshine Mining Company stock, I thought it advisable to write this letter. It was understood that this stock was to be purchased by the Yakima Holding Corporation and held by it for the account of the bank. The Yakima Holding Corporation was to be reimbursed for the amount actually paid for the stock, plus a small appreciation to be determined at the end of the year if this should be deemed necessary. We, therefore, treated this stock as being held for the bank, and if any loss results it is to be the loss of the bank and, of course, if any profit results it will likewise accrue to the bank.

"I am taking this opportunity also of setting out the understanding reached in connection with the proposal submitted by us to Mr. Alexander Miller to exchange 4000 shares of stock of the Yakima Holding Corporation for 5000 shares of stock of the Sunshine Mining Company. We are doing this on the express understanding that stock of the Sunshine Mining Company will be taken over by the bank at the stipulated price of $12.00 per share. This understanding is to apply to any further similar transactions.

"I would ask you to signify that this is also in accordance with your understanding of these transactions by signing the acknowledgment on the bottom of this letter.

Yours very truly,
GEO. H. BRADSHAW
Secretary

GHB:M

"The above represents the understanding that has been reached between the bank and the Yakima Holding Corporation with respect to the matters set out above, and the same is hereby approved.

YAKIMA FIRST NATIONAL BANK

By H. F. CRAWFORD
Cashier"

At the request of Mr. Hardy the foregoing letter was

approved in writing on behalf of the Bank by its cashier Mr. Crawford, for the reason that he was the only officer of the Bank who was in no way connected with the Holding Company.

Although Mr. Bradshaw and Mr. Miller died prior to the trial, the testimony of Mr. Hardy, Mr. Rightmire and Mr. Crawford is definite, positive and unequivocal that this letter was actually written and signed on the date that it bears, December 12, 1934. The testimony is further undisputed that the letter was signed, approved and delivered before Mr. Miller left about the middle of December to spend the winter in California where he remained until the following spring. (Tr. 82-89, 106-107, 142, 157-8, 164-5, 244)

These two transactions were further confirmed by the minutes of the Holding Company executive committee meeting on April 12, 1935, which read in part as follows:

> "A meeting of the executive committee of the Yakima Holding Corporation was held in the office of the Yakima First National Bank on Friday, April 12, 1935, at 3:00 P. M.
>
> "There present Messrs. Hardy, Bradshaw, Rightmire and Clift.
>
> "Mr. Hardy stated there were several matters that required action by the executive committee and stated that the first matter was a proposal to Mr. Alex Miller to exchange 4000 shares of stock of the Yakima Holding Corporation for 5000 shares of Sunshine Mining Company stock on the basis of placing a value of $15.00 per share on the stock of the Holding Corporation and $12.00 per share on the stock of the Sunshine Mining

Company. This proposal was made to Mr. Miller under date of December 11, 1934 and accepted by him. It was then moved by Mr. Clift, seconded by Mr. Rightmire, that we approve and ratify the proposal for the exchange of stock as outlined and authorize its completion. Carried.

"The secretary then stated that at the time this transaction with Mr. Miller was discussed by the officers an understanding was reached that if the transaction were completed that the Yakima First National Bank would take over from the Yakima Holding Corporation the 5000 shares of Sunshine at $15.00 per share; also the 7500 shares of Sunshine stock already owned by the Yakima Holding Corporation at the cost price of same, all in accordance with a letter setting out this understanding dated December 12, 1934 from the secretary to the bank and approved by the bank.

"It was then moved by Mr. Rightmire, seconded by Mr. Clift, that the arrangement between the Holding Corporation and the Bank as outlined by the secretary be approved and ratified, which motion being put was unanimously approved.

"The secretary then pointed out that it would be necessary to issue some new stock to Mr. Miller in fulfillment of the transaction and that inasmuch as the price fixed for the sale of capital stock had been previously fixed at $20.00 per share, it would be necessary to have a resolution approving the issuance of any new stock at $15.00 per share. It was then moved by Mr. Bradshaw, seconded by Mr. Rightmire, that in order to consummate certain plans of reorganization that had been under consideration by the officers of the company for some time that it was necessary that some additional stock of the corporation be disposed of and that in view of changed economic conditions it would be necessary to fix a lower price than the $20.00 per share provided for in previous issues of stock and that we now authorize the issuance of such additional stock as may be necessary to complete the transaction with Mr. Miller at a price of $15.00 per share, and also authorize the dis-

posal of such other stock as may be necessary to carry out the contemplated plans of reorganization at a price of $15.00 per share. This motion being put was unanimously approved."

(Pl. Ex. 15, Tr. 167, 308)

It is undisputed that the use of the figure $15.00 per share in reference to the said 5000 shares of Sunshine stock was due to inadvertent mistake, the correct amount being $12.00 per share, and the Miller transaction was carried out on that basis. (Tr. 488)

As to the 5000 shares no entry whatever was made on the Holding Company's books until the exchange was actually consummated and the stock sold in April 1935. Mr. Miller continued to receive the dividends thereon. (Tr. 183) The Holding Company never received any dividends, income or profit whatsoever therefrom. (Tr. 183) The entire profit realized from the sale thereof was paid to the Bank. Said Miller stock was never in the possession of the holding company.

For obvious reasons, in view of the limitations in the national bank statutes, no entries were made in the books and records of the Bank until the stock was sold. At that time all of the profit on the sale of the stock was actually received and retained by the Bank. (Tr. 64-69, 78, 79, 139, 141, 248-9) The records of the Bank so showed, and the Bank reported the full amount of profit as income in its 1935 income tax return. (Pl. Ex. 26 ,Tr. 327, 351) These matters were discussed at several meetings of the executive

committee of the Bank, but as was the custom, no minutes were kept of such meetings. (Tr. 134)

Pursuant to the original oral agreement, the Holding Company received and retained for its services in connection with the matter the dividends amounting to $1500 paid upon the 7500 shares of Sunshine stock. Also pursuant to the original oral agreement the Holding Company received as compensation an "appreciation write-up" in the sum of $1875, being at the rate of 25c per share on the 7500 shares. Entry thereof was made on the Holding Company books on January 6, 1935. (Tr. 122, 129, 149, 159) The market value of the stock at that time of course had advanced much more than that amount. The Holding Company was actually paid this amount out of the proceeds of the sale of the stock at the time of the sale. (Tr. 202, 317) The Holding Company reported in its 1935 income tax return the said $1500 dividend it received and the $1875 "appreciation write-up" or compensation received by it. (Pl. Ex. 28, Tr. 367, 387, 390, 392) With that exception the full amount of the profit realized on both of these stock transactions was actually received by the Bank and was reported by it in its 1935 income tax return. (Pl. Ex. 26, Tr. 327, 351)

The entries in the Holding Company books with reference to the 7500 shares, as stated in the findings of fact entered by the District Court, "have as specifically designated items on the ledger page the initials Y. F. N. B. for the description of the number of shares and the price paid

for each share." (Tr. 488) This designation of course referred to Yakima First National Bank as the beneficial owner of the stock. (Tr. 33, 35, 36, 118, 193-5, 202-205, 254, 284)

In the latter part of April 1935, the market value of the stock having greatly advanced, and the bank examiner having continued to urge that the financial affairs of the Bank be promptly placed in better condition, 11,000 shares of the 12,500 shares in question were sold for the total sum of $199,225.45. For that purpose all of the stock certificates were *delivered by the Bank* to Drumheller, Ehrlichman & White, a Seattle stock brokerage concern, having a branch office at Yakima. Payment for the stock was made by Drumheller *directly to the Bank.* (Tr. 64-69, 78-9, 107, 108, 135, 141) It is undisputed that if the Holding Company had been the owner of the stock, in accordance with its uniform custom and practice it would have sold the stock through Guaranty Trust Company, where it had its office. (Tr. 115-118) However, this was not done, and the stock was delivered and sold by the Bank. The stock was property of the Bank, and not of the Holding Company. (Tr. 107, 108, 114, 115, 124, 128, 131, 135, 254)

The selling price of the 7500 shares was $135,835.54. The cost of this stock to the Bank, including the $1875 "appreciation write-up" or compensation paid by the Bank to the Holding Company, was $61,451.50, making a gross profit in the sum of $74,384.04 received and retained by the Bank as to the 7500 shares.

At the same time at the request of the Bank Drumheller sold 3500 shares of the 5000 shares of Miller stock for $63,389.91, net proceeds of sale; the cost or purchase price thereof was $42,000, leaving a profit on the 3500 shares in the sum of $21,389.91. The remaining sum of $77,773.95 was retained by the Bank and reported in its 1935 income tax return. (Tr. 320, 324, 327, 351) The remaining 1500 shares of Sunshine stock were *redelivered by the brokers to the Bank and retained by it* until later sold in 1938. (Tr. 57, 64, 320) Later in 1935 the Bank was sold to the National Bank of Commerce of Seattle. (Tr. 89)

It is undisputed that none of the stock involved in either transaction ever stood in the name of the Holding Company. Tr. 25, 256, 257) The 5000 Miller shares were transferred directly from Miller to the Bank. (Pl. Ex. 2, Tr. 25, 257)

Out of the proceeds of the sale in April 1935, the Bank paid Miller for the 5000 shares of Sunshine stock at the agreed basis of $60,000 and the Bank paid the Holding Company the amount which the latter had paid for the 7500 shares and the 25c per share "appreciation write-up" thereon, in the total sum of $61,451.50, all in accordance with the oral agreement of August 1934 and the written agreement of December 12, 1934. (Tr. 317, 491) The income or profit on all of the stock, both the 7500 block and the 3500 block, was actually received and retained by the Bank and was reported by it in its 1935 income tax return. (Tr. 64-69, 7819, 233, 320, 324, 327, 351) The agreement was actually carried out and performed in accordance with the letters

of December 11 and 12, 1934. (Tr. 143, 315)

With reference to the Miller transaction, the evidence clearly establishes, and the District Court made further findings as follows:

> "The transaction with Alex Miller with reference to the 5000 shares of Sunshine stock was originally in December, 1934, and at all times, made, agreed upon, consummated and put through for the benefit of the Bank. The reason for the method used in handling the transactions was that the parties realized the restrictions upon national banks in the purchase of stock in corporations. The transactions were not handled in that manner in order to evade or reduce payment of income taxes of either the Bank or the Holding Company.
>
> "The court finds that the said 5000 shares of Sunshine stock was acquired from Alex Miller for the Bank, and the Holding Company acted in a trust capacity for, or as agent of, the Bank and that at all times until the sale thereof the actual, equitable and beneficial owner and holder of the said 5000 shares of Sunshine stock was the Yakima First National Bank and was not the Holding Company." (Tr. 492)

With reference to the 50% fraud penalty, the District Court made the following findings:

> "That there was no fraud or bad faith on the part of any of the said corporations or their officers or agents with reference to any of the transactions involved herein, and no fraud or bad faith in making any of the income tax returns of any of said corporations for the year 1935. At the time the said income tax returns for 1935 were made, the Holding Company, its officers and agents, did not know that it owed any taxes upon income derived from any of the transactions involved herein, and bona fidely believed that all of the profit belonged to the Bank, and said taxpayer did not fraud-

ulently or knowingly fail to report any income or profit derived from any of the transactions involved herein. That by reason thereof, no fraud penalty could properly be assessed against any of said corporations, including the Holding Company, with reference to any of the transactions involved herein. There was no wrongdoing on the part of any of the said corporations, including the Holding Company, or its officers or agents, in connection with any of the transactions involved herein, and there was no purpose or intention on the part of the Holding Company or its officers or agents or any of the corporations referred to herein to evade any tax believed by said parties to be owed to the defendant; and there was no fraudulent intent whatsoever by any of said parties with reference thereto." (Tr. 493)

It is admitted by the pleadings that thereafter in 1937 the Commissioner of Internal Revenue made a deficiency assessment against plaintiff for 1935 income and excess profits taxes in the sum of $16,515.51, plus 50% fraud penalty thereon in the sum of $8,257.76, or a total of $24,773.27. Plaintiff made written sworn protest and presented affidavits, but the protest was denied. On May 27, 1938, plaintiff paid defendant the said sum of $24,773.27 plus interest thereon in the sum of $2160.59 to said date, or a total payment of $26,933.86. Thereafter plaintiff filed claims for refund, which were denied. (Tr. 11, 17, 494)

The foregoing statement of the case closely follows the findings of fact entered by the District Court (Tr. 480) and is clearly supported by the evidence, which in practically all respects is undisputed.

As hereinabove stated, the court held in favor of the

defendant as to the profit on the 7500 shares and in favor of the plaintiff as to the profit on the 3500 Miller shares and as to the fraud penalty, and entered judgment in favor of plaintiff for $12,793.04, together with interest and costs, (Tr. 498) from which both parties have appealed. (Tr. 499, 505)

SPECIFICATION OF ERRORS

The District Court erred:

1. In making finding of fact No. 10 (Tr. 489), the same being merely an erroneous conclusion as to the 7500 share transaction.

2. In making finding of fact No. 27 (Tr. 495), as the same erroneously disallows recovery as to the 7500 share transaction.

3. In making conclusion of law No. 2 (Tr. 497), as the same erroneously disallows recovery as to the 7500 share transaction.

4. In making conclusion of law No. 3 (Tr. 497), as the same erroneously disallows recovery as to the 7500 share transaction.

5. In entering judgment in favor of the plaintiff for only the sum of $12,793.04, together with interest and costs (Tr. 498), in that said recovery is inadequate because the same does not include recovery as to the 7500 share transaction.

6. In failing and refusing to enter judgment in favor of the plaintiff for the full amount sued for, to-wit, $26,933.86, together with interest and costs. (Tr. 15)

7. In holding that said 7500 shares of Sunshine stock were not purchased and held by the Holding Company as trustee or agent for the Bank, and that the equitable and beneficial owner thereof was the Holding Company, and that the entire profit thereon was taxable to the Holding Company and not to the Bank, and in holding and concluding that plaintiff is not entitled to recover herein the tax paid based on the profits from the sale of said 7500 shares of Sunshine stock.

8. In failing and refusing to hold that plaintiff is entitled to recover herein, in addition to the amount of the judgment entered, all taxes and interest paid by virtue of the profits on the sale of said 7500 shares of Sunshine stock.

ARGUMENT

1.

SUMMARY OF ARGUMENT

Our position in this case is clear, simple and well founded upon undisputed evidence. Not only the Miller 5000 shares of Sunshine stock, but also the 7500 shares, were purchased by the Holding Company as agent for and held in trust for the Bank. The sole, equitable, beneficial owner thereof, the cestui que trust was the Bank. If the Holding Company had any title at all to the stock, it was solely a

bare legal title as trustee for the Bank. The Holding Company having advanced out of its own funds the purchase price of the stock as to the 7500 shares, was of course entitled to be reimbursed by the Bank for the funds so advanced, and naturally the stock was being held as security for such repayment.

The whole question in this case is: Could the Holding Company in May 1935 or thereafter have recovered this profit from the Bank? The answer is obvious. It could not. The Holding Company was bound morally, equitably and legally by its solemn agreement, both oral and in writing, that the stock should be held in trust for the Bank and that the Bank should be and was the sole, equitable and beneficial owner thereof and that the Bank was entitled to the profit realized therefrom. The agreement was undoubtedly valid and binding upon the Holding Company. Being valid and binding upon the taxpayer, it is elementary that the same was valid and binding upon the government for tax purposes. The same was therefore properly reported as income of the Bank and not income of the Holding Company.

It never was and never was intended to be income of the Holding Company, and therefore was not properly taxable as such. It never was received by the Holding Company. It never was claimed by the Holding Company. It was received and retained by the Bank. Everyone at all times

agreed and recognized that the Bank was the owner and entitled to the profit so realized.

If as we contend and as we believe the evidence conclusively establishes, both the 7500 shares and the 5000 Miller shares were held in trust for the Bank, then it necessarily follows, and is we believe undisputed, that plaintiff is entitled to recover herein the full amount sued for, $26,933.86, together with interest and costs, the same being the amount of taxes and penalty illegally assessed and collected by the Commissioner from the plaintiff.

Stipulation has been filed, approved by this court, for consolidation of these two appeals for argument in the briefs and otherwise. The greater portion of this brief will discuss our appeal, but at the close thereof we shall briefly discuss the questions presented upon defendant's appeal relative to the Miller stock and the fraud penalty. Most of the argument herein is applicable to both the 7500 share and the 5000 share transactions.

2.

EFFECT TO BE GIVEN TO DISTRICT COURT'S FINDINGS OF FACT

An extremely important preliminary question, applicable to both appeals, relates to the effect to be given to the findings of fact entered by the District Court. (Tr. 480) The District Court had the supreme advantage of seeing and hearing the witnesses testify and observing their de-

meanor on the witness stand, which of course is wholly impossible for this court in judging the case upon the cold printed record.

Every finding of fact made by the District Court as to both the 7500 share and 5000 share transactions is favorable to the plaintiff with the single exception of finding No. 10 which is purely a conclusion (that the profit on the 7500 shares constituted income of the Holding Company) *and the amount of recovery stated in finding No. 27 which is likewise purely a conclusion.* As previously stated, the foregoing statement of the case herein is taken largely from the court's findings of fact.

The two following rules as to the effect to be given to the findings of the trial court are well settled:

1. Findings of fact entered by the trial court relative to the basic facts themselves will not be set aside if supported by substantial evidence.

2. Findings of fact which are actually mere inferences or conclusions are not binding upon the appellate court and will be set aside if erroneous.

Each of these principles is directly applicable here. As to the facts themselves, all of the findings of fact entered by the trial court are, to say the least, supported by more than substantial evidence. As a matter of fact they are supported by overwhelming, undisputed evidence. Consequently those findings as to the facts cannot be set aside or reversed by this court.

On the other hand, those findings which actually are merely conclusions and inferences of the district court, namely, the conclusion that the profit on the sale of the 7500 shares was taxable to the Holding Company and not to the Bank and constituted income of the Holding Company and not the Bank, are not binding upon this court. The conclusions of the district court as to the 7500 shares are clearly erroneous and therefore should be reversed.

Rule 52(a) of the Federal Rules of Civil Procedure, 28 U. S. C. A. following sec. 723c, contains the following provision:

> *"Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge of the credibility of the witnesses."*

In the recent case of *Wittmayer v. United States,* 118 F. (2d) 808, this court said:

> "After a careful examination of the record we are unable to say that the Court's findings are clearly erroneous. Rule 52(a), Federal Rules of Civil Procedure, 28 U. S. C. A. following section 723c. . . .
>
> "The findings of the trial Court fall within the familiar rule, that where based upon conflicting evidence they are presumptively correct, and unless some obvious error of law, or mistake of fact, has intervened, they will be permitted to stand. *Silver King Coalition Mines Co. v. Silver King C. M. Co.,* 8 Cir., 204 F. 166, 177, Ann. Cas. 1918B, 571.
>
> "The provisions of the new procedural rules that the findings of fact of the trial judge are to be accepted on appeal unless clearly wrong (Rule 52(a), 28 U. S. C. A. following section 723c), is but the formulation of

a rule long recognized and applied by courts of equity. *Guilford Const. Co. v. Biggs,* 4 Cir., 102 F. (2d) 46, 47.

"As was said by Mr. Justice Holmes in *Adamson v. Gilliland,* 242 U. S. 350, 353, 37 S. Ct. 169, 170, 61 L. Ed. 356 (citing *Davis v. Schwartz,* 155 U. S. 631, 636, 15 S. Ct. 237, 39 L. Ed. 289), the case is pre-eminently one for the application of the practical rule, that *so far as the findings of the trial judge who saw the witnesses 'depends upon conflicting testimony or upon the credibility of witnesses, or so far as there is any testimony consistent with the finding, it must be treated as unassailable.'* "

In *Missouri Pac. Trans. Co. v. George,* (C. C. A. 8) 114 F. (2d) 757, the court said:

"The findings are based upon conflicting testimony. The appellants' contention is that the quoted finding is not supported by a preponderance of the evidence. We have examined the evidence, and *the quoted finding is supported by substantial evidence. It is not, therefore, clearly erroneous. It can not for that reason be set aside by this court.* Rule 52(a), Rules of Civil Procedure."

In *Storley v. Armour & Co.,* (C.C.A. 8) 107 F. (2d) 499, 513, Judge Sanborn speaking for the court said:

"The plaintiffs, in appealing, seem to have assumed that this Court, the jurisdiction of which is appellate, would, in effect, retry the issues which were tried in the court below and would substitute its judgment as to damages for that of the trial court. This is a misconception. It is not the function of this Court to retry this case and to pass upon questions of fact the determination of which depended upon the credibility of witnesses and the weight of evidence, or to substitute its judgment for that of the trier of the facts which had reached permissible conclusions. See *Helvering v. Johnson,* 8 Cir., 104 F. (2d) 140, 144, and cases cited, and Rule 52(a) of the Rules of Civil Procedure

for the District Courts of the United States, 28 U. S. C. A. following section 723c."

In *Jensma v. Sun Life Assurance Co.*, 64 F. (2d) 457, this court said:

"The appellees concede that even in a case of this character the appellate court had the power to consider the evidence, but insist that *such examination must not go farther than to inquire 'whether there is any evidence to support the findings and whether the findings support the judgment.'*

"*This is unquestionably the law.* In *Dooley v. Pease*, 180 U. S. 126, 131, 132, 21 S. Ct. 329, 331, 45 L. Ed. 457, the court said:

'Where a case is tried by the court, a jury having been waived, its findings upon questions of fact are conclusive in the courts of review, it matters not how convincing the argument that upon the evidence the findings should have been different. *Stanley v. Supervisors* (of Albany County), 121 U. S. 547, 7 S. Ct. 1234, 30 L. Ed. 1000, 1002.

'Errors alleged in the findings of the court are not subject to revision by the circuit court of appeals, or by this court, if there was any evidence upon which such findings could be made.' (Citing numerous cases.) . . .

"We will therefore test the foregoing finding No. IV according to the rule laid down in section 875, supra; namely, 'when the finding is special the rule may extend to the determination of the sufficiency of the facts found to support the judgment.' We will also inquire whether, under the undisputed testimony, there was any substantial evidence upon which the lower court might have based an assumption that the infection from which the insured died was caused by other than 'external means.' Finally, we will endeavor to determine whether, as a matter of law, the finding

of the lower court, on its face, does not establish the fact that the 'means' were 'accidental'."

See also to the same effect:

Sundt v. Turman Oil Co., (C. C. A .5), 107 F. (2d) 762, 764, and cases cited;

Crowell v. Baker Oil Tools, (C. C. A. 9), 99 F. (2d) 574, 577, and cases cited;

Clarke & Wilson Lumber Co. v. McCallister, (C. C. A. 9), 101 F. (2d) 709, 714;

State Farm Mutual Automobile Ins. Co. v. Coughran, (C. C. A. 9), 92 F. (2d) 239;

Oliver v. Bell, 103 F. (2d) 760;

American Home Fire Ins. Co. v. Hargreaves, 109 F. (2d) 86.

The following authorities, among many others, discuss *both* of the rules hereinabove referred to:

In *Campana Corporation v. Harrison*, (C. C. A. 7), 114 F. (2d) 400, 405, also a tax case, the court said:

"In the application of Federal Rule 52 it is the following principle that guides this Court: the reviewing court does not review the evidence as an original fact finding tribunal; it does not attempt to settle conflicts in evidence or to determine questions of credibility. In re Duvall, 7 Cir., 103 F. (2d) 653, 655; *Guilford Const. Co. v. Biggs*, 4 Cir., 102 F. (2d) 46, 47. Of course Federal Rule 52 does not require us to accept fact findings unsupported by the evidence. *Nor does this Rule require us to respect conclusions of law which do not rest properly on the facts so found. It is certain that the principle giving the above described weight to the trial court's findings of fact, does not compel the reviewing court to give any specific weight to the trial court's conclusions of law, as it yet remains the duty*

of the appellate court to decide whether the correct rule of law has been applied to the facts found. Whether special findings are supported by the evidence or whether they give the requisite support to conclusions rendered thereon, are questions open to consideration here."

In *Kuhn v. Princess Lida*, (C. C. A. 3), 119 F. (2d) 704, the court said:

"The appellee reminds us that we are not at liberty to disturb findings of fact made by the trial court unless they are unsupported by evidence or are otherwise clearly erroneous. Rule 52(a), 28 U. S. C. A. following section 723c. The reason for the rule rests in large part upon the fact that the trial judge who hears the witnesses testify and observes their demeanor upon the stand is better qualified to appraise the credibility of their testimony and to resolve the conflicts therein. So long, therefore, as a finding of fact is supported by evidence and is not clearly erroneous, it is to be accepted on appeal as verity.

"*The rule does not operate, however, to entrench with like finality the inferences or conclusions drawn by the trial court from its fact findings. And so, while accepting the facts competently found by the trial court as correct, an appellate court remains free to draw the ultimate inferences and conclusions which, in its opinion, the findings reasonably induce.* Such was the law prior to the promulgation of the Rules of Civil Procedure. *Brown v. United States*, 3 Cir., 95 F. (2d) 487, 490; *Dunn v. Trefry*, 1 Cir., 260 F. 147, 148. The new rules have worked no change in this regard, or with respect to the ultimate conclusions in jury-waived cases in particular. Cf. *Aetna Life Insurance Co. v. Kepler*, 8 Cir., 116 F. (2d) 1, 5. See also 3 Moore, Federal Practice, p. 3115, et seq., and notes of the Advisory Committee on Rule 52(a). The sufficiency of the evidence to sustain a trial court's conclusion or finding of an ultimate fact remains appropriate matter for an appellate court's consideration. *State Farm*

Mutual Automobile Insurance Co. v. Bonacci et al., 8 Cir., 111 F. (2d) 412, 415. Where the evidentiary facts are not in conflict or dispute, *the conclusions to be drawn therefrom are for the appellate court* upon review of the trial court's action. Cf. *United States v. South Georgia Railway Co.*, 5 Cir., 107 F. (2d) 3, and *United States v. Mitchell*, 8 Cir., 104 F. (2d) 343, 346. *An incorrect conclusion by a trial court qualifies as a 'clearly erroneous' finding, for the correction whereof on appeal Rule 52(a) specifically provides.*"

It follows therefore that on both of these appeals this court is bound by the findings of fact entered by the trial court as to the facts themselves, but is not bound by the conclusions and inferences of the trial court, even though included among the findings of fact, and the same in so far as erroneous should be reversed. As to the correct inferences and conclusions to be drawn from the facts found by the trial court and shown by the overwhelming evidence herein, and hereinabove summarized, we submit that only one proper conclusion can be drawn, namely, that the equitable, beneficial owner of the 7500 shares, as well as the 5000 shares, was the Bank and not the Holding Company, and consequently that the entire gain as to the 11,000 shares sold was taxable solely to the Bank. The case therefore should be reversed upon plaintiff's appeal and affirmed upon defendant's appeal.

3.

HOLDING COMPANY HELD THE STOCK IN TRUST OR AS AGENT FOR THE BANK

This is the principal, if not the only, question in this case as to both appeals. We do not believe there can be the slightest doubt as to the correctness of our conclusions. The Holding Company purchased the 7500 shares of Sunshine stock in August 1934 and held the same in trust or as the agent of the Bank pursuant to oral agreement then made. It was so testified by Messrs. Hardy, Rightmire, and Crawford. (Tr. 82-89, 93-97, 143, 156-159, 164-5, 170-1) They were the only surviving officials of these two corporations who handled these transactions, Messrs. Bradshaw and Miller having died prior to the trial.

Not a single witness has testified to the contrary. Defendant introduced no evidence whatsoever having any direct or material bearing upon the basic questions involved. The only witnesses called by defendant were William Bradshaw, the son of George H. Bradshaw, and A. J. Cooke. Bradshaw testified that at that time he was merely a bookkeeper for the Holding Company and made entries in the books thereof as instructed from time to time by his father, George H. Bradshaw. (Tr. 186, 192-5, 204-5) Defendant's only other witness was A. J. Cooke, a national bank examiner, who made examinations of this Bank from time to time. Mr. Hardy testified that he told Cooke about

these two stock transactions in December 1934 and in certain telephone conversations during the following few months. (Tr. 127-135, 145-6, 159-166, 179-181) This was denied by Cooke, who claimed that the first time he learned of this was during his examination of the Bank in June 1935.

Obviously it is wholly immaterial for tax purposes whether Cooke ever knew about this transaction. The trial court expressly stated in its opinion that it considered this conflict in the testimony of no moment whatever and that it would therefore purposely refrain from making any finding or conclusion thereon. (Tr. 462) In this the District Court was clearly right, as the dispute was of no moment or importance whatever.

On the other hand, Cooke's testimony directly corroborates and strengthens our position in that he testified directly in accord with plaintiff's witnesses that from time to time he as national bank examiner was urging Mr. Hardy and the Bank that the same be placed in better financial condition either through issuance of preferred stock to the R. F. C. or otherwise, to avoid an impairment of capital due to a number of doubtful assets acquired in the merger with First National Bank, of which Mr. Miller was a large stockholder. (Tr. 220-228, 233, 236-240, 242-252) This directly coincides with plaintiff's testimony upon the point, and shows the motive and purpose behind these entire transactions, namely, a desire to improve the financial con-

dition of the Bank. Under the undisputed evidence that was the sole purpose of both of these stock transactions, namely, to benefit the Bank by improving its financial condition and thereby to satisfy the national bank examiners without the necessity of issuing preferred stock to the R. F. C. (Tr. 97-101, 139, 144, 220, 246)

It is apparent therefore that defendant's evidence, so far as material at all, directly supports plaintiff's position in this case. Not a single witness has testified to the contrary.

The undisputed testimony of Messrs. Hardy, Rightmire and Crawford also conclusively establishes that the important letter of December 12, 1934, (Pl. Ex. 19, Tr. 47, 315) was prepared and signed by Mr. Bradshaw for the Holding Company and Mr. Crawford for the Bank on the date that it bears, December 12, 1934. (Tr. 82-89, 106, 107, 142, 157-8, 164-5, 244) Not a single witness has testified to the contrary. This was more than four months before the sale of the stock. The letter was signed before Mr. Miller went south to California for the winter, which occurred before Christmas 1934. (Tr. 157-8)

This letter, (Pl. Ex. 19, Tr. 315), has been hereinabove quoted in full and the same clearly and unequivocally establishes that all of this stock was purchased and held by the Holding Company *"for the account of the Bank."* The same further provides:

"We therefore treated this stock as being held for the

bank, and if any loss results it is to be the loss of the bank, and of course if any profit results it will likewise accrue to the bank."

It is perfectly obvious that thereafter no court would have listened for a moment if the Holding Company had ever endeavored to make the contention that it and not the Bank was the beneficial owner of this stock or was entitled to the profit realized from the sale thereof. The Holding Company was conclusively bound by its solemn, written signed agreement, and the same is likewise of course binding upon the government for tax purposes.

In its "detailed opinion of the court on the facts" (Tr. 450, 463, 464), the court said:

> "The testimony of Mr. Hardy, Mr. Rightmire and Mr. Crawford is that the foregoing letter and acceptance were written and signed on December 12, 1934, for the purpose of reducing to writing the understanding between the Holding Company and the Bank as to the two transactions. Each of the witnesses is a reputable citizen of Yakima. There was nothing in the demeanor of any of these witnesses on the stand nor was anything elicited by the cross examination to deprecate the value of the testimony. . .
>
> "Mr. Hardy, Mr. Rightmire and Mr. Crawford were not impeached upon cross examination nor was there anything in their demeanor on the stand which would detract from the force of their testimony. . . .
>
> "I give full weight to the testimony of Mr. Hardy and Mr. Rightmire and Mr. Crawford. Particularly, do I do this because I know Mr. Hardy and have great respect for his integrity."

Again in the "opinion of the court" (Tr. 466) the court said:

"The oral testimony of plaintiff was submitted by Mr. Hardy, Mr. Rightmire, the treasurer of the corporations, and Mr. Crawford, the cashier of the Bank. Four of the men who actively participated in the transactions herein involved died between 1934 and the time of trial. The three witnesses who did testify are highly reputable citizens of Yakima. The testimony was given in such a way as to merit consideration by the Court."

In paragraphs 6 and 12 of its formal findings of fact later entered, the District Court said in part:

"That on December 12, 1934, an agreement was entered into between the Holding Company and the Bank, executed in the form of an accepted letter, as follows: " (then follows a copy of the letter—Pl. Ex. 19)

"That on December 12, 1934, the Holding Company by its secretary, George H. Bradshaw, wrote the letter to the Bank which is quoted above in paragraph 6. The foregoing agreement was executed and delivered on December 12, 1934, and was performed." (Tr. 484, 490)

It is undisputed that *none of the 7500 shares were ever held in the name of the Holding Company.* Of the 7500 share block, 5000 shares were taken and held *in the name of the Bank* and 2500 shares in the name of George H. Bradshaw, who was the secretary of the Holding Company and also a director and member of the executive committee of the Bank. The evidence to this effect is undisputed. (Pl. Ex. 1, 5, Tr. 25, 256, 267) and the court so found. (Tr. 484)

It is also undisputed that this agreement, originally oral and later confirmed in writing and signed by both parties, was scrupulously carried out by all parties. In April 1935 when the 11,000 shares of stock were sold, all of

the stock certificates *were delivered by the Bank* to Drumheller, Erhlichman & White, stock brokers, who sold the stock and *paid the purchase price to the Bank.* The Bank then reimbursed the Holding Company for its disbursements for the purchase price of the stock and for the agreed "appreciation write-up" in the sum of $1875, as the Holding Company's compensation in addition to the dividends previously received on the 7500 shares, and *the Bank retained all of the remaining profits realized on both transactions.* The brokers *delivered to the Bank* a certificate for the remaining 1500 shares and the same *was retained by the Bank* until sold in 1938. These facts are clearly established by the undisputed evidence (Tr. 64-69, 78-9, 107-8, 135, 141) and the court so found. (Tr. 489 to 492)

Naturally no entry was made with reference to either transaction on the Bank's books until the stock was sold and the profit realized, for two obvious reasons: (1) Under the national bank statutes it was admittedly improper for the Bank to own and hold the Sunshine stock. (2) The Bank at that time had not paid for the stock. Consequently there is nothing about that fact which in any way detracts from plaintiff's position. As hereinabove stated, the entry in the books of the Holding Company as to the 7500 share transaction had a designation written thereon, "YFNB", thereby designating the Bank's connection with the transaction. (Tr. 33, 35, 36, 118, 193-5, 202-5, 254, 284)

Consequently both the undisputed evidence and the

substantial evidence in the case conclusively establish and the trial court expressly found that the Holding Company and the Bank through their respective officers in 1934 made a trust agreement, originally oral and thereafter confirmed in writing and signed by both parties, that the 12,500 shares of Sunshine stock were to be held in trust for or as agent of the Bank and that the Bank would be entitled to the profit realized therefrom, and that this agreement was completely and literally carried out and performed by all parties. What more could anyone ask for as to conclusive proof of a trust relationship? *Manifestly a trust agreement, oral and written, entered into by both parties and performance thereof by both parties are conclusive as to the trust relationship.*

4.

EXPLANATION OF FACTS RELIED UPON BY DEFENDANT

What then are the facts relied upon by defendant as against this overwhelming mass of evidence?

1. Defendant and the trial court in its opinion rely strongly on the fact hereinabove stated that on January 6, 1935, entry was made in the Holding Company books as to the $1875 "appreciation write-up", although the stock had not yet been sold, and also that the Holding Company received and retained the dividends on the 7500 shares.

The answer to this is obvious. That was the agreed

compensation which the Holding Company was to receive for its services in handling the transaction and for its advancement of the money for the purchase price. *The fact that the entry was made before the stock was sold is of no moment whatever as indicating the equitable ownership of the stock in the Holding Company.*

On the contrary, it clearly corroborates plaintiff's position. The Holding Company had a lien upon the stock for its advances and services. In order that its books should clearly show the amount of its lien or interest, the "appreciation" had to be entered on its books.

Of course the money had not been received by the Holding Company at that time, the entry could not be properly made if the Holding Company was the absolute owner of the stock for its own benefit, it would have been a fraudulent entry.

As stated in the District Court's opinion:

> "The compensation the Holding Company was to receive for the use of this substantial part of its assets was to be the dividends which might be declared upon the mining stock while the Holding Company was holding it, plus a small write-up which might be allowed to the Holding Company if the joint officers deemed it advisable. It was agreed that any profits which might accrue upon the stock would be the profits of the Bank and that any losses upon the stock would be the losses of the Bank." (Tr. 476)

The original agreement was very definite and explicit that this "appreciation write-up" was to be determined

"at the end of the year" 1934. The letter of December 12, 1934, (Pl. Ex. 19, Tr. 315) definitely provides:

> "The Yakima Holding Corporation was to be reimbursed for the amount actually paid for the stock, plus a small appreciation *to be determined at the end of the year* if this should be deemed necessary."

This entry in the books was made early in 1935, shortly after the end of the year 1934, and *was directly in accord with the agreement* between the Holding Company and the Bank, and at that time became a liquidated amount due and had to be entered on the books. The very fact that this entry was made in the books admittedly on January 6, 1935, is additional evidence which strongly overwhelms the ridiculous contention of the defendant, wholly unsupported by anything whatever in the evidence, that this whole matter was purely an after-thought devised in April 1935 when the stock was sold. The books of the Holding Company themselves show that as early as January 6, 1935, the parties were actually engaged in carrying out the definite terms of their agreement.

2. The fact that no mention hereof appears in the minutes of either corporation as to any meeting of the board of directors, executive committee or stockholders until April 12, 1935.

This, however, is merely a lack of certain additional corroborating evidence, but is not a weakness of any substantial moment in plaintiff's case, and certainly does not establish defendant's contention. The evidence is clear,

definite and undisputed that frequent meetings of the executive committee of the Holding Company and the Bank were held and that as a rule no minutes were kept of such meetings. (Tr. 134) Also that this matter was discussed and authorized at such meetings in 1934. The officers of the Bank were present and had personal knowledge that the Holding Company had duly authorized and approved this transaction, and they had no fear that the Holding Company would violate this solemn agreement. Especially so when the Holding Company did not have possession of the stock and 5000 shares of the first 7500 block was in the name of the Bank. Eventually these transactions were definitely approved in the official records of the meeting of the Holding Company executive committee on April 12, 1935, which was two or three weeks prior to the sale of the stock. (Pl. Ex. 15, Tr. 308)

Under the by-laws the action of the executive committee was binding upon the corporation where rights of third parties were affected. (Pl. Ex. 15, Tr. 297)

Some reliance is also placed on an expression used in the minutes of April 12, 1935, (Pl. Ex. 15, Tr. 309) "also the 7500 shares of Sunshine stock already owned by the Yakima Holding Corporation." However a reference to the context shows that the minutes had just been referring to the Miller stock which *had not* yet been paid for by the Holding Company nor transferred from Miller. This was merely an expression used to differentiate the 7500 shares

which *had* already been fully paid for by the Holding Company and transferred from the original owner into the name of the Bank and Bradshaw. The Holding Company had ownership in the sense that it had legal title. That the same was subject to a trust in favor of the Bank, and that the Bank was the holder of equitable title and entitled to the full benefit of the profits to be realized, is shown by the context and by the reading of the minutes as a whole, as well as the letter of December 12, 1934, therein specifically referred to and approved. We submit that it is absurd to pick out one isolated clause written by a layman when the document read as a whole leaves no doubt whatever that the entire beneficial interest in both transactions was in the Bank and not the Holding Company.

3. Reliance is also placed upon the fact that the financial statement of the Holding Company under date of January 7, 1935, which was read at the annual stockholders' meeting on February 5, 1935, contained the item: "other stock investments, $61,451.50," and the minutes show no specific reference to this transaction.

This entry, however, was perfectly proper. The Holding Company had made an investment which, including the $1875 "appreciation write-up" amounted to that exact figure, $61,451.50. It was an investment in stock which had actually been made by the Holding Company out of its own funds, although borrowed from the Bank. The Holding Company's interest, investment, claim or lien on or in the

stock amounted to $61,451.50, and no more. And that is an investment. It was in fact at that time a substantial asset of the Holding Company by reason thereof, and this does not in any way negative the beneficial ownership thereof by the Bank as cestui que trust, in fact confirms it.

If A makes an arrangement with B, a broker for example, that B shall purchase and pay for ten shares of American Telephone stock, and that B shall advance the money for the purchase price thereof, and shall hold the stock as security and in trust for A, and that A shall bear the loss if the stock goes down and be entitled to the profit if the stock goes up, manifestly the broker B has a substantial interest and investment in the stock until his advances are repaid. But this does not in any way negative the fact that A has a beneficial interest as cestui que trust and is entitled to the profit if the stock goes up, upon reimbursement of B for the purchase price and compensation for his services.

1 Scott on Trusts, sec. 12.10, p. 104; 2 Restatement Trusts sec. 448.

The management of the corporation was vested in the board of directors and the executive committee. Approval of these transactions by the stockholders was wholly unnecessary. Explanation of these transactions to the stockholders would have inevitably resulted in such publicity that the same would have become a matter of public information, and in those troublous depression days of Feb-

ruary 1935 would have probably resulted in a run on the Bank. Under the by-laws submission of such matters to the stockholders for ratification was discretionary with the board of trustees, (Pl. Ex. 15, Tr. 295) and certainly under these circumstances the board did not abuse its discretion in electing not to do so.

Of course, as hereinabove stated, no entries were made in the Bank's books prior to the sale of the stock (1) in view of the limited powers of national banks under the statute, and (2) because the Bank at that time had not paid for the stock.

We might mention in passing that *Geddes v. Anaconda Mining Co.*, 254 U. S. 590, was referred to in the court below as requiring fairness in transactions between corporations having interlocking directorates. This principle, however, is not germane to any of the issues involved on these appeals. There is not the slightest suggestion in the evidence of any unfairness to any party involved. Obviously the stockholders of the Holding Company were vitally interested as much as anyone in putting the Bank in good standing with the national bank examiners, as they through the Holding Company owned all of the stock of the Bank except qualifying shares. These transactions were for the best interests of the stockholders of the Holding Company in benefiting the Bank, of which indirectly they were the owners. No stockholder or creditor of the Holding Company is or ever has complained.

This concern for the stockholders of the Holding Company is somewhat ironical when the party expressing the concern is attempting to mulct them out of thousands of dollars. It is their money plaintiff is attempting to recover for their benefit.

The Holding Company was bound by its agreement, as all of the parties well knew. The interest of the Bank was shown by the designation "YFNB" appearing opposite these entries in the books of the Holding Company, which was an admission binding upon the latter. Even if, however, it be considered that the Holding Company's books did not fully show the interest of the Bank, the books would be deemed self-serving declarations of the Holding Company, and of course not binding on the Bank.

22 C. J. 220, sec. 193, and cases cited.

4. Finally it is suggested that the Holding Company had no legal power to act as trustee.

True, its articles of incorporation do not expressly use that term. They do, however, contain extremely broad grants of power which we submit were sufficient to permit it to engage in these two isolated transactions directly for the benefit of the Bank of which it owned all of the stock:

> "The objects and purposes of the formation of this corporation are to establish a holding company to take and hold the capital stock of banks, trust companies, corporations, joint stock companies and associations, and generally to hold corporate stocks, bonds and obligations . . . To buy, own, hold, purchase, receive or acquire, and to sell, negotiate, guarantee, assign, deal

in, exchange, transfer, mortgage, pledge or otherwise dispose of *shares of capital stock, issued by banks, trust companies or other corporations, . . . and to do any acts or things designed to protect, preserve, improve or enhance the value of any such shares, . . .* To organize, incorporate, re-organize, finance and *to aid and assist financially or otherwise,* companies, corporations, joint stock companies, syndicates, partnerships and associations of all kinds, *particularly those engaged in banking,* or in other financial enterprises, and to underwrite, subscribe for and endorse the bonds, stocks, securities, debentures, notes or undertakings of any such companies, corporations, joint stock companies, syndicates or associations, or to make any guarantees in connection therewith or otherwise for the payment of money or for the performance of any obligation or undertaking, *and to do any and all things necessary or convenient to carry any of such purposes into effect.*

. . . "To undertake and carry on any business, undertaking, enterprise, venture, transaction or operation generally undertaken or carried on by promoters, contractors and merchants, and in the course thereof, to acquire and dispose of or otherwise to turn to account or realize upon all or any negotiable or transferrable instruments or securities. . . . *To loan money and to take as evidence of any security* for money loaned, notes, mortgages, deeds of trust, bonds, debentures or *other choses in action. . . . To do any and all acts and things necessary and convenient to the attainment of the purposes for which this corporation is organized,* or any of them, and to the same extent as natural persons lawfully could do in any part of the world in so far as such acts are permitted to be done by a corporation organized under the laws of the State of Washington." (Pl. Ex. 15, Tr. 289-294)

Under the circumstances shown here these isolated transactions were reasonably incidental to the business of the Holding Company as a holding company and hence were not ultra vires.

1 Scott on Trusts, sec. 96.3, p. 509;;

Latshaw vs. Western Townsite Co., 91 Wash. 575, 158 P. 248;

Mercy v. Hall & Son, Inc., 177 Wash. 338, 31 P. 2d 1009;

First University Investment Corp. v. Roosevelt Savings & Loan Assn., 170 Wash. 444, 16 P. 2d 820;

Castle & Co. v. Public Service Underwriters, 198 Wash. 576, 89 P. 2d 506.

Of course the law of the State of Washington governs, both because this transaction occurred there and this was a Washington corporation.

Erie Ry. Co. v. Tompkins, 304 U. S. 64, 82 L. Ed. 1188, 114 A. L. R. 1487.

Moreover under the law of Washington, as well as that generally recognized, the Holding Company would have been clearly estopped to assert any claim of ultra vires in view of the partial performance and the benefits received from the transactions:

Creditors Claim & Adjustment Co. v. Northwest Loan & Trust Co., 81 Wash. 247, 142 Pac. 670, L.R.A. 1917 A 737, Ann. Cas. 1916D 551;

Flannagin v. American Minerals Producing Co., 108 Wash. 569, 185 Pac. 609;

First University Investment Corp. v. Roosevelt Savings & Loan Assn., 170 Wash. 444, 16 P. 2d 820;

Castle & Co. v. Public Service Underwriters, 198 Wash. 576, 89 P. 2d 506;

Union Fruit Producers v. Plumb, 1 Wn. (2d) 378, 95 P. 2d 1033;

Frost v. Puget Sound Realty Assn., 57 Wash. 629, 107 Pac. 1029;

Tootle v. First National Bank, 6 Wash. 181, 33 Pac. 345;

Korn v. Spokane Trust Co., (C.C.A. 9) 276 Fed. 68;

Equitable Trust Co. v. Washington-Idaho Light & Power Co., 300 Fed. 601, 614.

The defendant in this case cannot raise the issue of ultra vires; it has no standing in court for such a purpose.

13 Am. Jur., sec. 759, p. 790.

Besides, the law is well established:

"*Even though a corporation is not expressly authorized by its charter or certificate of incorporation to engage in the business of administering trusts, it is within its corporate power to administer trusts for such purposes as are germane to the purposes for which it is created.*"

1 Scott, Trusts, sec. 96.3, p. 509;

Latshaw v. Western Townsite Co., 91 Wash. 575, 158 P. 248.

We therefore conclude that the facts relied upon by the defendant are trivial and unimportant, and that the overwhelming weight of the evidence in this case conclusively shows that both of these blocks of stock were purchased and held by the Holding Company in trust for the Bank.

5.

AUTHORITIES ESTABLISH TRUST RELATIONSHIP

The legal principles applicable to this trust relationship

between these parties are elementary, well settled, and have been repeatedly recognized by this court.

The authorities clearly establish that a trust relationship existed here.

Adamson v. Black Rock Power & Irrigation Co., (C.C.A. 9) 297 Fed. 905;

Portland Cremation Assn. v. Commissioner, (C. C. A. 9) 31 F. 2d 843;

26 R. C. L. 1182 therein cited;

Chicago, etc., Ry. Co. v. Des Moines, etc. Ry Co., 254 U. S. 196, 65 L. Ed. 219, 41 S. Ct. 81, therein cited;

O'Meara v. Commissioner, (C.C.A. 10) 34 F. 2d 390;

Foreman v. Foreman, 251 N. Y. 237, 167 N. E. 428;

Tucker v. Brown, 199 Wash. 320, 92 P. 2d 221;

Holmes v. Holmes, 65 Wash. 572, 118 Pac. 733.

For convenience of the court quotations from these authorities will be found in the appendix herein.

That the arrangement between Bank and Holding Company created a fiduciary relation with all the characteristics, rights and obligations of a trust and vested in the Bank all of the beneficial interest in the Sunshine stock, is too clear for argument.

1 Restatement, Trusts, sec. 8, comment f, and sec. 24;

1 Scott on Trusts, sec. 8, p. 65.

When property is brought by A for "the account" of B, that being the language of the letter of December 12, 1934, (Pl. Ex. 19, Tr. 315) all of the beneficial interest belongs

to B. The legal title may be in either, or a third party, and possession may be in either or a third party. When the legal title or possession is in A or a third party, A has a security interest in the property for his advances, if any, and his services. When something is done "for" your account or similar words, it clearly shows that the person was acting in a representative capacity, the word "for" meaning "on behalf of."

Donovan v. Welch, 90 N. W. 262, 264.

An endorsement of a check "for the account of" B creates a trust in favor of B and the holder of the check is a trustee.

Freeburg v. Stoddart, 28 Atl. 1111;

White v. Miners National Bank, 102 U. S. 658, 661, 26 L. Ed. 250;

First National Bank of Belmont v. First National Bank of Ramesville, (Ohio) 50 N. E. 723, 724.

Stock bought by A for the account of B belongs to B. A however has a security interest and if A has possession or title, he has it as pledgee or trustee for B.

12 C.J.S. 74, sec. 29;

9 C. J. 542-3, sec. 45.

Under the undisputed evidence in this case hereinabove referred to and under the foregoing well settled principles, there cannot be any doubt whatever that this stock was held in trust by the Holding Company for the Bank.

6.

PRESUMPTION OF COMMISSIONER'S CORRECTNESS WAS FULLY OVERCOME BY THE EVIDENCE

Defendant, having no substantial evidence upon which to rely, is forced to rely upon the presumption as to the correctness of the Commissioner's deficiency assessment, and contends that that should be thrown into the scales to be considered as substantial evidence. We believe that to some extent the District Court was probably misled by this contention. (Tr. 469, 470)

That defendant's contention has no merit is well settled. It is elementary that in the absence of evidence the presumption favors the defendant which relies upon a ruling of the Commissioner in such cases; but it is equally well settled that when the plaintiff introduces substantial evidence to overcome the presumption of correctness of the Commissioner's ruling, the presumption then entirely disappears from the case and is not to be weighed in the scales as evidence.

This court removed all doubt upon the question in *Ariasi v. Orient Insurance Co.*, 50 F. 2d 548, involving the presumption that officers acted rightly in the performance of their legal duties in revoking a winery permit, and hence that wine thereafter in the possession of the permitee was illegally possessed, the question arising in a suit to recover under a fire insurance policy for its loss. This court said:

"The question for our consideration then is, did the testimony of the appellant directly controverting this prima facie evidence of illegal possession require the trial court as a matter of law to find the fact to be as he testified them to be? Although there is a fundamental rule of law that a trial court is not required to accept the testimony of any witness as true, but must weigh the testimony of such witness in connection with all the other evidence in the case and determine the truth, *in the absence of all contradictory evidence and any inherent improbability in the testimony, the court cannot arbitrarily reject the testimony of a witness whose testimony appears credible.* . . .

"The difficulty with this claim is that although this conclusion was required in the absence of any evidence to the contrary, *the prima facie effect of the revocation is dissipated by positive evidence to the contrary. It does not constitute evidence to be placed in the scale and weighed as against the positive evidence of the plaintiff* to the effect that he did not intend to violate the law and had not done so."

In *New York Life Ins. Co. v. Gamer,* 303 U. S. 161, 82 L. Ed. 726, 58 Sup. Ct. 500, 114 A.L.R. 1218, the court said:

"*The presumption is not evidence and ceases upon the introduction of substantial proof to the contrary.* . .

"The evidence being sufficient to sustain a finding that the death was not due to accident, there was no foundation of fact for the application of the presumption; and the case *stood for decision* by the jury *upon the evidence unaffected by the rule* that from the fact of violent death, there being nothing to show the contrary, accidental death will be presumed. *The presumption is not evidence and may not be given weight as evidence.*"

See also the numerous federal cases to the same effect therein cited. The court further said that with the

presumption eliminated the question should be determined *"by the greater weight of evidence."*

In *Del Vecchio v. Bowers,* 296 U. S. 280, 80 L. Ed. 229, 56 Sup. Ct. 190, the court said:

> "Once the employer has carried his burden by offering testimony sufficient to justify a finding of suicide, *the presumption falls out of the case. It never had and cannot acquire the attribute of evidence in the claimant's favor. Its only office is to control the result where there is an entire lack of competent evidence.* If the employer alone adduces evidence which tends to support the theory of suicide, the case must be decided upon that evidence. Where the claimant offers substantial evidence in opposition, as was the case here, the issue must be resolved upon the whole body of proof pro and con."

In *Cooperative Publishing Co. v. Commissioner,* 115 F. 2d 1017, a tax case, this court reversed a decision of the Board of Tax Appeals and directed entry of a new order *"without relying upon the presumption in favor of the Commissioner's finding that such assets had no cost, as that presumption was fully overcome by the evidence."*

In *Seaside Improvement Co. v. Commissioner,* (C.C.A. 2) 105 F. 2d 990, a tax case, cited by this court in the Cooperative Publishing case, the court said:

> *"Once the taxpayer had introduced evidence* as to the basic value, *the presumption was out of the case."*

In *Paul v. United Ry. Co.,* 152 Mo. App. 577, 134 S. W. 3, quoted with approval in *Beeman v. Puget Sound T. L. & P. Co.,* 79 Wash. 137, 139 Pac. 1087, the court said:

" '*Presumptions*' as happily stated by a scholarly counselor ore tenus, in another case, '*may be looked on as bats of the law, flitting in the twilight but disappearing in the sunshine of actual facts.*' That *presumptions have no place in the presence of actual facts* disclosed to the jury, or where plaintiff should have known the facts had he exercised ordinary care, is held in many cases of which samples are, *Reno v. Railroad,* 180 Mo. 1. c. 483; *Nixon v. Railroad,* 141 Mo. 1. c. 439; *Bragg v. Railroad,* 192 Mo. 331. To give place to presumptions on the facts of this case is but to play with shadows and reject substance."

In *Sullivan v. Associated Dealers,* 4 Wn. (2d) 352, 103 P. (2d) 489, the court said:

"We have held so many times that it would seem to need no citation of authority that this *presumption is not evidence, and relates only to a rule of law as to which party shall first go forward and produce evidence* to sustain the matter in issue; that it will serve in the place of evidence only until prima facie evidence has been adduced by the opposite party; and that *the presumption should never be placed in the scale of evidence.*"

See also to the same effect:

Bradley v. Savage, Inc., 13 Wn. (2d) 28, 123 P. (2d) 780;

Anning v. Rothschild & Co., 130 Wash. 232, 226 Pac. 213;

Scarpelli v. Washington Water Power Co., 63 Wash.18, 114 Pac. 870;

Peters v. Lohr, (S.D.) 124 N. W. 853;

Caswell v. Maplewood Garage, 84 N. H. 241, 149 Atl. 746, 73 A.L.R. 433;

Fiocco v. Carver, 234 N. Y. 219, 137 N. E. 309 (by Judge Cardozo);

Phillip v. Schlager, 214 Wis. 370, 253 N. W. 394;

Watkins v. Prudential Insurance Co., 315 Penn. 497, 173 Atl. 644, 95 A. L. R. 869, and numerous cases cited in the annotation thereto at page 878;

Weiget v. Becker, (C.C.A. 8) 84 F. 2d 706;

Albrecht & Son v. Landy, Collector, 114 F. 2d 202;

Massachusetts Bonding & Ins. Co. v. Hudspeth, 94 F. 2d 467;

Equitable Life Assur. Soc. v. McDonald, (C.C.A. 9) 96 F. 2d 437, certiorari denied, 305 U. S. 624;

Flannery v. Wilcuts, 25 F. 2d 951:

"Inferences or presumptions speak in the absence of evidence, but cannot be weighed in the balance as against evidence."

Guaranty Trust Co. v. Minneapolis & St. Louis R. Co., (C.C.A. 8) 36 F. 2d 747, certiorari denied, 281 U. S. 756.

In *Department of Water and Power v. Anderson,* (C. C. A. 9) 95 F. 2d 577, 583, certiorari denied, 305 U. S. 607, this court said:

"If the opposing party complies with the presumption or procedural rule of law, and introduces evidence, the presumption thereafter has no application or function, and disappears entirely."

7.

CLEAR AND CONVINCING EVIDENCE UNNECESSARY

The District Court erroneously held (Tr. 470) as contended by defendant that clear and convincing evidence is

necessary to overcome such presumption. That this is not the law is clearly established by the numerous authorities cited above. When evidence is introduced, the presumption is taken out of the case and the question is to be determined as in all cases by the preponderance of the evidence. In this case we did introduce clear and convincing evidence, in fact conclusive evidence, to show the error of the Commissioner. The District Court erred, however, in holding that clear and convincing evidence was necessary. The cases cited were misinterpreted and actually make no such holding.

Of the four cases cited in the court's opinion (Tr. 470) *Pearce v. Commissioner,* 315 U. S. 543, 86 L. Ed. 1016, and *Helvering v. Fitch,* 309 U. S. 149, 84 L. Ed. 665, involved a special rule applicable to a special situation, namely, whether ex-husband or ex-wife was liable for income tax based on alimony payments after the divorce. The presumption in such cases is so strong that the husband is liable for the tax in such cases because of his continuing obligation to support the ex-wife, that the special rule has arisen that the husband has the burden of showing by clear and convincing evidence that the Commissioner is wrong if he so holds. On the other hand, the wife (the Pearce case involves only the wife) sustains her burden "merely by showing doubt and uncertainty as to whether the payments were made pursuant to her former husband's continuing obligation to support her." In the Pearce case the husband purchased and paid for an annuity insurance policy payable

to the wife and the Supreme Court held that the ex-wife, who was the beneficiary thereof, and not the ex-husband, was liable for the tax on income received therefrom, as she was in effect the beneficial holder thereof. It will thus be seen that actually the Pearce case directly supports our position in this case rather than the contrary.

There is not the slightest suggestion in either of these cases that clear and convincing evidence is necessary as a general rule in order to overcome the presumption of the correctness of the Commissioner's ruling.

The other two cases cited, *Welch v. Helvering,* 290 U. S. 111, 78 L. Ed. 212, and *Wickwire v. Reinecke,* 275 U. S. 101, 72 L. Ed. 184, merely refer to said presumption of correctness and that the burden of proof is upon the taxpayer, but *do not hold* that clear and convincing evidence is necessary. It is recognized in these cases and the cases cited therein, as well as those cited under the preceding subdivision of this brief, and in fact every case on the subject of which we are aware, except a few cases involving the special husband and wife relationship, that clear and convincing evidence is not necessary and that the general rule as to the controlling effect of the preponderance or greater weight of the evidence controls.

8.

ILLEGALITY NO DEFENSE

The answer of the defendant contains no affirmative

defense, such as illegality or ultra vires. It is elementary that such defense to be available must be affirmatively pleaded in the answer. Federal rule 8c so requires.

It is of course well settled—and this was no doubt the reason for not pleading the same—that the illegal nature of a transaction is wholly immaterial upon a question of income tax liability.

Angelus Building & Investment Co. v. Commissioner, (C.C.A. 9) 57 F. 2d 130, certiorari denied, 286 U. S. 562;

Penn v. Robertson, (C.C.A. 4) 115 F. 2d 167, 172-175, and the decision of the District Court in the same case therein affirmed, 29 F. Sup. 386;

Becker v. Scofield, (C.C.A. 9) 221 F. 322, affirmed 243 U. S. 114, 61 L. Ed. 626;

Huston v. Drake, (C.C.A. 9) 97 F. 2d 863, 867;

Hamburg Bank v. Onacheita National Bank, (C.C.A. 8) 78 F. 2d 100, 105.

U. S. v. Sullivan, 274 U. S. 259, 71 L. Ed. 1037, 54 A.L.R. 1020;

Steinberg v. U. S., (C.C.A. 2) 14 F. 2d 564.

In the *Angelus* case, *supra,* this court said:

> "*The government in the collection of its revenues takes no notice of any situation of accountability to a state that the taxpayer may have caused to exist through his own wrongdoing.* His transactions are as he has made them, and, if real income credits have been created which are subject to be taxed, they are to be assessed accordingly."

There was, however, nothing illegal about this transaction. The same was merely ultra vires and in excess of

the powers of the Bank. The distinction between ultra vires and illegality is fundamental and well settled. In *Williston on Contracts* (Rev. Ed.) Vol. 1, page 787, sec. 271, the learned author says:

> "Practically all revisions of corporate statutes have adopted the agency theory (as to ultra vires), but *the distinction between ultra vires and illegality remains.*"

Again in Vol. 6, page 5027, sec. 1770 of the same work Williston says:

> "Reference may also be made here to ultra vires contracts of corporations. *Lack of corporate capacity should not be confused with illegality.*"

The only pertinent provisions of the national bank statutes, as amended June 16, 1933, 12 U.S.C.A. 24 (7) are as follows:

> ". . . The business of dealing in investment securities by the association shall be limited to purchasing and selling such securities without recourse, solely upon the order, and for the account of, customers, and in no case for its own account, and the association shall not underwrite any issue of securities. . . .
>
> "Except as hereinafter provided or otherwise provided by law, nothing herein contained shall authorize the purchase by the association of any shares of stock of any corporation." . . .

It will be noted that it is recognized in the act that a national bank does not have lawful power to purchase stock in corporations, but there is no positive prohibition thereof, the same is not declared to be illegal, and no penalty is imposed therefor. Clearly therefore these transac-

tions, although ultra vires as to the Bank and therefore voidable by it, were not illegal ad were not void. The District Court in its opinion (Tr. 471) correctly said:

> "There is no serious difference between the parties in the opinion that since this law contains no positive prohibition against the purchase of corporate stocks by a National bank that a bank's contract to purchase stock is not illegal and void, but is ultra vires and voidable. *Lantry v. Wallace,* 182 U. S. 536; *First Nat. Bank v. Stewart,* 107 U. S. 676. That being true, plaintiff's contention that in this case 'The Bank could not lose. If the price went up it could enforce the deal against the Holding Company. If it went down it could refuse to perform,' must be accepted as a correct statement of the legal consequences of the situation."

Compare the foregoing section with 12 U. S. C. A. 83, being the act of 1864 which provided:

> "No association shall make any loan or discount on the security of the shares of its own capital stock, nor be the purchaser or holder of any such shares", etc.

Obviously if under the 1864 statute a purchase of the Bank's own shares is merely ultra vires and not illegal or void, a fortiori the same must be true that a purchase by a bank of stock in another corporation cannot be more than merely ultra vires.

In *Lantry v. Wallace,* 182 U. S. 536, 45 L. Ed. 1218, the court said:

> "In view of these decisions *it cannot be held that the purchase by the bank of its own shares of stock was void.* It was of course a matter of which the government by its officers could take cognizance; and it may be that it was a matter of which stockholders, having

an interest in the proper administration of the affairs of the bank, could complain in a proceeding instituted by them to restrain the bank from violating the statute. But when the violation of the statute has occurred, it is not a matter of which a shareholder can complain in order that he may be relieved from the liability attaching to him as a shareholder and which the receiver seeks to enforce under the orders of the Comptroller. In the present case Judge Thayer, delivering the opinion of the circuit court of appeals, well said: 'In considering the second defense which was interposed by the defendant, it is important to bear in mind that the 200 shares of stock which he purchased from the bank was not void stock, but was stock which, according to the averments of the answer, had once been issued to other persons, and had been reacquired by the bank by purchasing it from such other persons, to prevent them from throwing it on the market at ruinous prices. It is necessary to infer from the averments of the answer that this stock had once passed the scrutiny of the Comptroller and had been outstanding and had been held by other persons since the organization of the bank in the year 1891. *The purchase of this stock by the bank under the circumstances disclosed by the answer was doubtless ultra vires, but the purchase in question did not render the stock void.* In purchasing it the bank made an unlawful use of its funds for which the officers concerned in the transaction could have been held responsible, as for any other unlawful act, if the corporation had sustained damage; but in point of fact, by the sale of the stock to the defendant, that portion of its capital which had been dissipated by the purchase was restored by the resale, and no loss seems to have been incurred. We are at a loss to understand how this transaction on the part of the bank can operate to relieve the defendant from his liability as a stockholder in a suit brought by the receiver to recover a stock assessment which was levied solely for the benefit of corporate creditors. The sale of the stock to the defendant after the bank had purchased the same was not unlawful, since it operated to restore that part of the capital that had been retired,

and to that extent repaired the wrong which might otherwise have been done to the bank's creditors.' 38 C. C. A. 510, 514, 97 Fed. 865, 868."

In *First National Bank v. Stewart,* 107 U. S. 676, 27 L. Ed. 592, the court said:

"While this section, in terms, prohibits a banking association from making a loan upon the security of shares of its own stock, it imposes no penalty, either upon the bank or borrower if a loan upon such security be made. If, therefore, the prohibition can be urged against the validity of the transaction by anyone except the government, it can only be done before the contract is executed, while the security is still subsisting in the hands of the bank. It can then, if at all, be invoked to restrain or defeat the enforcement of the security. When the contract has been executed, the security sold, and the proceeds applied to the payment of the debt, the courts will not interfere with the matter. Both bank and borrower are in such case equally the subjects of legal censure, and they will be left by the courts where they have placed themselves."

The foregoing cases were cited with approval in *Oppenheimer v. Harriman National Bank,* 301 U. S. 206, 81 L. Ed. 1042.

In *The Seattle,* (C. C. A. 9), 170 Fed. 284, 287, this court said:

"The law has imposed no penalty upon a national bank for its failure to obey the restriction, unless it be that its charter thereby becomes subject to forfeiture under section 5239. A court may not inflict penalties other than those which are imposed by statute. The bridge company could have made no defense in the present case on the ground that the bank had violated the statute. *Gold Mining Co. v. National Bank,* 96 U. S. 640, 24 L. Ed. 648."

If a loss had occurred, Mr. Miller, who was the moving spirit, and the bank officers, Messrs. Hardy, Rightmire and Crawford, were personally liable to the bank.

McKinnon v. Mosse, 177 Fed. 576;

Cooper v. Hill, 94 Fed. 582;

Atherton v. Anderson, 86 F. 2d 518; 526-7 (remanded on another point, 302 U. S. 643);

12 U. S. C. A. 93.

In *Jackman v. Continental National Bank,* (C. C. A. 8) 16 F. 2d 728, 51 A. L. R. 336, 344, after a review of the authorities, the court said:

> "The gist of these decisions, therefore, is that debtors, borrowers, and private parties generally, cannot complain of such unwarranted exercise of power by national banks, particularly after the power has been exercised to the extent of a sale of the securities and an application of the proceeds, and that, as against the bank itself, the government alone can interfere, by proceedings in ouster and dissolution."

See also to the same effect:

9 C. J. S. 1220, 1243, sec. 664, 665, 688, and cases cited;

National Bank v. Matthews, 98 U. S. 621, 25 L. Ed. 188;

12 U. S. C. A. 93;

First National Bank v. Shewalter, (Mo.) 134 S. W. 12;

First National Bank v. Smith, 65 N. W. 437.

Clearly therefore the Holding Company could not have refused to carry out its agreement because the transaction was ultra vires as to the Bank. The transaction was valid, lawful and binding except voidable by the Bank

if there was a loss. Otherwise the question could only be raised by the government in a quo warranto proceeding. Both transactions having shown a large profit, no one was injured and no one was in a condition to complain because the same were ultra vires as to the Bank. Obviously this would not affect the income tax liability of either the Bank or the Holding Company.

9.

PROFIT ON SALE OF STOCK WAS TAXABLE TO BANK AS BENEFICIAL OWNER

As we understand, defendant does not dispute the legal proposition that if the Holding Company purchased and held this stock as trustee or agent for the Bank, the gain derived from the sale thereof is of course properly taxable to the Bank as beneficial owner and not to the Holding Company. This principle is of course well settled.

112 West 59th Street Corporation v. Helvering, (C. A. D. C.) 68 F. 2d 397, is directly in point. The court said:

> "In *Central Life Society v. Commissioner,* 51 F. 2d 939, 941, the Court of Appeals in the Eighth Circuit, speaking through Judge Stone, said: 'Tax laws are essentially practical in their purposes and application, and the federal income tax laws are no exception. While for purposes of convenience and certainty in collection of such taxes, it is sometimes provided that those who collect income for others shall pay therefrom the taxes thereon, yet *a cardinal purpose of the income tax laws is to tax the income to the person who has the right or beneficial interest therein, and not to throw*

the burden upon a mere collector or conduit through whom or which the income passes.'

"We think this a correct statement of the law. If, therefore, it appears, as we think it does appear, that petitioner was a mere 'conduit' and that it never at any time had any legal right to retain the profits from the transaction in question and never at any time had possession of such profits, but that on the contrary the profits in right and in law were always the property of the trust, then it would seem to follow that the liability to pay the tax under the federal income tax laws was solely a liability of the trust and not a liability of petitioner. And this is particularly true when we consider that the former duly reported and paid the tax and no question of bad faith in the organization of petitioner or in its participation in the transaction is or can be attributed to it. The brief of the Commissioner frankly says 'there is no fraud here.'

"That petitioner on the admitted facts is a mere trustee is beyond question. If the contest instead of involving a tax, were a contest between petitioner and the trust, it would be unconscionable to argue that, because the property was taken in petitioner's name, it could claim a beneficial ownership therein. It may well be that at the time of the transaction there was no specific or formal agreement that petitioner should hold the property for the benefit of the trust, but *the absence of such agreement or the lack of formality does not alter the obvious intent of the arrangement.* No court would in the circumstances we have named permit it to retain the property or the profits in fraud of the real owner. Petitioner is a New York corporation, and the doctrine we have stated is that recognized and enforced by the courts of that state. . . .

"The corporation thus created furnished the structure for the taking and the holding of the legal title and the channel through which to pass it when the sale was made, but it furnished nothing more. It had no other function and performed none. It held the legal title, but it recognized at all times that the equit-

able title was in the trust. In such circumstances the Tax Board has many times held that *no income accrues to the person in whose name the property is so held.* Stewart Forshay, 20 B.T.A. 537; Greenleaf Textile Corp., 26 B.T.A. 737; Moro Realty Corp., 25 B.T.A. 1135. In the latter case, the Board's decision was affirmed without opinion by the Court of Appeals in the Second Circuit (65 F. 2d 1013). . . .

"It cannot be that the mere absence of an express agreement to hold the property as trustee can be said to be conclusive of the negative of that relationship. The question is rather one of fact, and, as we have seen, the facts proved and found by the Board irrefragably show the true nature of the transaction to have been a naked trusteeship."

See also to the same effect:

Central Life Assurance Society v. Commissioner, (C. C. A. 8) 51 F. 2d 939;

Bettendorf v. Commissioner, (C. C. A. 8) 49 F. 2d 173;

Shellebarger v. Commissioner, (C. C. A. 7) 38 F. 2d 566;

Riker v. Commissioner, (C. C. A. 2) 42 F. 2d 150;

DeBrabrant v. Commissioner, (C. C. A. 2) 90 F. 2d 433;

U. S. v. Arnold, (C. C. A. 3) 89 F. 2d 246;

Johnson v. Commissioner, (C. C. A. 8) 88 F. 2d 952, 955, 956;

Letts v. Commissioner, (C. C. A. 9) 84 F. 2d 760;

Irwin v. Gavitt, 258 U. S. 161, 69 L. Ed. 897;

Byrne v. Commissioner, (C. C. A. 3) 110 F. 2d 294;

Sewell v. U. S. (Ct. of Claims) 19 Fed. Supp. 657;

Title Guarantee Loan & Trust Co. v. Commissioner, (C. C. A. 5) 63 F. 2d 621;

Mattern v. Commissioner, (C. C. A. 9) 61 F. 2d 663, 665;

Edmonds v. Commissioner, (C. C. A. 9) 90 F. 2d 14, cert. den. 302 U. S. 713;

Meeker v. Durey, (C. C. A. 2) 92 F. 2d 607;

Connery Coal & Investment Co. v. Commissioner, (C. C. A. 7) 84 F. 2d 485, 487;

White v. Ross, (C. C. A. 5) 73 F. 2d 236, 237;

Helvering v. Butterworth, 290 U. S. 365, 370, 78 L. Ed. 365, 368;

Commissioner v. Branch, (C. C. A. 1) 114 F. 2d 985, 132 A. L. R. 839;

Commissioner v. O'Donnell, (C. C. A. 9)90 F. 2d 907.

In *U. S. v. Spalding,* 97 F. 2d 701, cert. den. 305 U. S. 644, a tax case decided by this court, appellee Spalding made equitable assignment to Salisbury and Lovett of part of his beneficial interest in a certain oil lease agreement. This court held that income therefrom was taxable to the beneficial holders, Salisbury and Lovett, and that appellee Spalding was entitled to recover a refund from the government as to income tax paid by him based thereon. This court also distinguished *Lucas v. Earl* and similar cases which are relied upon by defendant herein, but which are clearly and obviously distinguishable upon the facts. Judge Mathews, speaking for this court, said:

"In determining appellee's tax liability for 1930, the Commissioner of Internal Revenue included as part of appellee's gross income the $17,765.64 which the Oil Company paid to Salisbury and Lovett in that year. Appellee contended that this was not income to him and should not have been so included. The trial court upheld appellee's contention and, we think, properly so. Salisbury and Lovett *were entitled to receive, and did receive, this money. It was not payable to or receivable by appellee, and was not so paid or received. It was not appellee's money, consequently, was not income of appellee. Blair v. Commissioner,* 300 U. S. 5, 11, 57 S. Ct. 330, 332, 81 L. Ed. 465.

"Cases cited by appellant *are readily distinguishable.* In *Lucas v. Earl,* 281 U. S. 111, 50 S. Ct. 241, 74 L. Ed. 731; *Wehe v. McLaughlin,* 9 Cir., 30 F. 2d 217; and *Daugherty v. Commissioner,* 9 Cir., 63 F. 2d 77, the taxpayer had, in each case, made an agreement with his wife whereby his future earnings were to be received and owned by them jointly. In *Ward v. Commissioner,* 9 Cir., 58 F. 2d 757, and in *Bing v. Bowers,* 2 Cir., 26 F. 2d 1017, the taxpayer had assigned future rentals, but had not assigned the lease or transferred the leased property, or any interest therein, to his assignee. In *Leydig v. Commissioner,* 10 Cir., 43 F. 2d 494, the claimed assignment was of royalties under oil and gas leases to be executed in the future. *These cases, obviously, are not in point."*

In *Blair v. Commissioner,* 300 U. S. 5, 81 L. Ed. 465, 57 S. Ct. 330, the court said:

"The Government points to the provisions of the revenue acts imposing upon the beneficiary of a trust the liability for the tax upon the income distributable to the beneficiary. But the term is merely descriptive of the one entitled to the beneficial interest. These provisions cannot be taken to preclude valid assignments of the beneficial interest, or to affect the duty of the trustee to distribute income to the owner of the beneficial interest, whether he was such initially or

becomes such by valid assignment. *The one who is to receive the income as the owner of the beneficial interest is to pay the tax.* If under the law governing the trust the beneficial interest is assignable, and if it has been assigned without reservation, the assignee thus becomes the beneficiary and is entitled to rights and remedies accordingly. We find nothing in the revenue acts which denies him that status. . . .

"The will creating the trust entitled the petitioner during his life to the net income of the property held in trust. He thus became the owner of an equitable interest in the corpus of the property. (Citing cases). By virtue of that interest he was entitled to enforce the trust, to have a breach of trust enjoined and to obtain redress in case of breach. The interest was present property alienable like any other, in the absence of a valid restraint upon alienation. (Citing cases). . . . The assignment of the beneficial interest is not the assignment of a chose in action but of the 'right, title and estate in and to property.' (Citing cases).

"We conclude that the assignments were valid, that *the assignees thereby became the owners of the specified beneficial interests in the income, and that as to these interests they and not the petitioner were taxable* for the tax years in question."

For the foregoing reasons the District Court was clearly in error in holding that the profit on the 7500 shares was taxable to the Holding Company and not to the Bank. The case should be reversed on plaintiff's appeal.

10.

MILLER STOCK WAS NOT TAXABLE TO HOLDING COMPANY

In closing we shall briefly refer to the Miller trans-

action and the fraud penalty which are involved on the defendant's appeal. There can be no question but that the District Court was clearly right in holding that the profit realized from the sale of the 3500 Miller shares was in any event clearly taxable to the Bank and not to the Holding Company. As to the Miller stock it will be borne in mind that this was never issued to the Holding Company and was never even in its possession. No written record whatever was made on the Holding Company books with reference to this stock. As to this stock the District Court in its opinion well said (Tr. 474):

> "I am convinced that the plaintiff has sustained its burden of proof as to the stock which was acquired from Alex Miller. As to that transaction the oral evidence is not contradicted by anything in writing. There were no entries made upon the Holding Company's books until after the transaction was completed and they were set up in such a way as to be susceptible of either interpretation. The only written evidence which detracts from this conclusion is in the minutes of the Holding Company's executive committee which provided that the Bank would take over the Miller stock at $15 a share instead of $12 a share as it later did. I have decided to resolve that doubt in favor of the plaintiff and to conclude that the use of the figure 15 was an error in the minutes. Having reached this conclusion, it follows that in so far as tax was levied on the profit accruing from the sale of the 3500 shares out of the Miller stock the assessment was erroneous."

The agreement as to the Miller stock is clearly shown by the written letters of December 11, 1934. (Pl. Ex. 16, 17, 18, Tr. 312). This agreement was fully carried out and

performed by all parties. With reference to this stock the District Court in its findings of fact expressly found:

> "No entries were made in the books of the Holding Company with reference to the Alex Miller transaction or the said 5000 shares of Sunshine stock; and the stock never stood in the name of the Holding Company.
>
> "That the income or profit on all of the stock, both the 7500 block and the 3500 block, was actually received and retained by the Bank.
>
> "The transaction with Alex Miller with reference to the 5000 shares of Sunshine stock was originally in December, 1934, and at all times, made, agreed upon, consummated and put through for the benefit of the Bank. The reason for the method used in handling the transactions was that the parties realized the restrictions upon national banks in the purchase of stock in corporations. The transactions were not handled in that manner in order to evade or reduce payment of income taxes of either the Bank or the Holding Company.
>
> "The transaction as to the 7500 shares of Sunshine stock and the said Alex Miller transaction as to said 5000 shares of Sunshine stock were at all times two separate and distinct transactions. The 5000 shares of Alex Miller Sunshine stock were never in the possession of the Holding Company.
>
> "The court finds that the said 5000 shares of Sunshine stock was acquired from Alex Miller for the Bank, and the Holding Company acted in a trust capacity for, or as the agent of, the Bank and that at all times until the sale thereof the actual, equitable and beneficial owner and holder of the said 5000 shares of Sunshine stock was the Yakima First National Bank and was not the Holding Company." (Tr. 490-492)

These findings of the court are clearly supported by the overwhelming and undisputed evidence in this case,

and the court's conclusions with reference thereto are clearly correct for the reasons and under the authorities hereinabove referred to.

11.

FRAUD PENALTY WAS ILLEGALLY ASSESSED BY COMMISSIONER

This is not an issue raised by defendant on this appeal under its statement of points. (Tr. 505, 518) As we understand, it is therefore not involved on either of these appeals. However, in passing we shall briefly refer to the facts and legal authorities supporting the court's conclusion that the 50% fraud penalty was illegally assessed by the Commissioner.

Under the statute, 26 U. S. C. A. 293b, a 50% fraud penalty may be imposed only "if any part of any deficiency *is due to fraud with intent to evade tax.*"

Here it is undisputed that there was no fraud on the part of anyone, and there was no intent to evade or reduce any tax whatsoever on the part of anyone. As to this the District Court in its detailed opinion on the facts (Tr. 464) well said:

> "Keeping in mind the nature of the fraud necessary to sustain the fraud penalty in a tax case, I can see no testimony of fraud here. The fraud referred to is the fraud in making the return. The standard is whether, at the time the return is made, the taxpayer knew that it owed the tax and fraudulently failed to report it. A transaction may be entirely fraudulent (I am not

saying that this one was) and still not support a fraud penalty. It did not appear to me from the argument of counsel for the defendant at the time of the trial or in the brief that defendant was seriously urging now that this fraud penalty should be sustained."

In its final opinion (Tr. 479) the District Court said:

"Plaintiff is entitled to recover the amount paid on the fraud penalty. On this question, the burden rests with the defendant. The fraud meant in the statute is actual, intentional wrong-doing and the intent required is the specific purpose to evade the tax believed to be owed. *Griffiths v. Commissioner,* 50 F. 2d 782; *Duffin v. Lucas,* 55 F. 2d 786; *Mitchell v. Commissioner,* 118 F. 2d 308. The defendant submitted no testimony on this point but asks me to conclude from the transaction that plaintiff must have had fraudulent intent at the time of making the return. Such a conclusion is not justified. After all, this income was reported. The report as to its receipt was made by the wrong company. While it may have been negligently made, that is not sufficient to support the conclusion of fraudulent intent."

In its findings of fact on this point the District Court found:

"That there was no fraud or bad faith on the part of any of the said corporations or their officers or agents with reference to any of the transactions involved herein, and no fraud or bad faith in making any of the income tax returns of any of said corporations for the year 1935. At the time the said income tax returns for 1935 were made, the Holding Company, its officers and agents, did not know that it owed any taxes upon income derived from any of the transactions involved herein, and bona fidely believed that all of the profit belonged to the Bank and said taxpayer did not fraudulently or knowingly fail to report any income or profit derived from any of the transactions

involved herein. That by reason thereof, no fraud penalty could properly be assessed against any of said corporations, including the Holding Company, with reference to any of the transactions involved herein. There was no wrong-doing on the part of any of the said corporations, including the Holding Company, or its officers or agents, in connection with any of the transactions involved herein, and there was no purpose or intention on the part of the Holding Company or its officers or agents or any of the corporations referred to herein to evade any tax believed by said parties to be owed to the defendant; and there was no fraudulent intent whatsoever by any of said parties with reference thereto." (Tr. 493)

See the authorities cited in the court's opinion, supra, and see also to the same effect the following:

Budd v. Commissioner, (C. C. A. 3) 43 F. 2d 782, 786;

DeLone v. Commissioner, (C. C. A. 3) 110 F. 2d 507, 509;

Rogers Recreation Co. v. Commissioner, (C. C. A. 2) 103 F. 2d 780, 782, 783;

Commissioner v. Woods Machinery Co., (C. C. A. 1) 57 F. 2d 635, 636, cert. den. 287 U. S. 613;

Jenison v. Commissioner, (C. C. A. 5) 45 F. 2d 4, 5, 6;

U. S. v. National City Bank, 21 Fed. Supp. 791, 797;

Hartford-Connecticut Trust Co. v. Eaton, (C. C. A. 2) 34 F. 2d 128, 130;

26 U. S. C. A. 1112.

Clearly therefore the District Court was right in finding and holding that there was no fraud, no intent to evade or reduce taxes, and consequently no right to assess the fraud penalty.

12.

ACTION LIES UNDER TUCKER ACT

It is, we believe, undisputed that if, as we have shown, these taxes and penalties were illegally assessed, plaintiff has a right to recover the same, together with interest, herein under the Tucker Act.

28 U. S. C. A. sec. 41 (20);

C. T. C. Investment Co. v. U. S., (C. C. A. 7) 108 F. 2d 383;

U. S. v. Bertelsen & Peterson Engineering Co., 306 U. S. 276, 83 L. Ed. 647, affirming 97 F. 2d 488 and 98 F. 2d 132;

U. S. v. Piedmont Manufacturing Co., (C. C. A. 4) 89 F. 2d 296, and cases there cited, affirming 15 Fed. Supp. 581;

A. S. Kreider Company v. U. S., (C. C. A. 3) 117 F. 2d 133, 137;

Moses v. U. S., (C. C. A. 2) 61 F. 2d 791, 793, cert. den. 289 U. S. 743.

We therefore respectfully submit that both the 7500 share and 5000 share blocks of stock were purchased and held by the Holding Company in trust for the Bank, or as agent for the Bank, that the Bank was the sole beneficial, equitable owner thereof, that the profit received by the Bank from the sale thereof was income of the Bank and therefore properly taxable to it and not to the Holding Company. The case should therefore be reversed on plain-

tiff's appeal and affirmed on defendant's appeal and judgment entered in favor of the plaintiff against the defendant for the full amount sued for, $26,933.86, together with interest thereon at 6% per annum from the date of payment, May 27, 1938, until paid, together with plaintiff's costs.

Respectfully submitted,

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APPENDIX

In *Adamson v. Black Rock Power & Irrigation Co.*, (C. C. A. 9) 297 Fed. 905, decree affirmed, 16 F. 2d 114, the instrument in question, although not expressly declaring a trust, provided that certain property was "pledged" for the performance of certain water right contracts. This court held that the property was subject to a perpetual trust for that purpose, saying:

> "As we view this instrument in the light of the circumstances of its execution and thereafter, the statements, reservations, stipulations, and contract therein constitute a declaration by the Hanford Company that it holds these instrumentalities in trust to the extent necessary for the purpose of water supply to prospective vendees of its lands, and that the vendees in the vendor settlor of the trust may repose confidence it forever will apply said instrumentalities to their use and benefit.
>
> "*It is hornbook law that trusts may be thus declared, or in several writings and less formal, or in writings not contemporaneous or not inter partes; that in creation they need no particular, formal, or technical words, no set phrases,* and require only that they be in praesenti, expressed in unequivocal language, admit of but one reasonable interpretation; and that settlor, intent, property, object, consideration and beneficiaries appear with reasonable certainty. This trust deed satisfies every requirement of equity to constitute a declaration of trust as aforesaid. *In so far as terms are concerned, they might be proven by parol,* and are found in the deeds of the lands to the vendees for whose benefit the trust was created."

Also directly in point is the decision of this court in the tax case of *Portland Cremation Assoc. v. Commissioner*

of *Internal Revenue,* (C. C. A. 9) 31 F. 2d 843. Deeds to patrons of the crematorium contained no reference to a maintenance fund, but pursuant to a resolution of the directors it was represented to purchasers that 20% of gross receipts would be set aside for perpetual care and maintenance of crematory urns. This court held that this constituted a trust and was therefore a proper deduction for income tax purposes. Judge Gilbert speaking for this court said:

> "*But a trust may be created by parol, and its creation does not depend on the use of particular words of trust. Chicago, etc., Ry. Co. v. Des Moines, etc., Ry Co.,* 254 U. S. 196, 208, 41 S. Ct. 81, 65 L. Ed. 219. *It may be inferred from facts and circumstances. Thus the owner and donor of personal property may create a perfect trust by his unequivocal declaration in writing or by parol that he himself holds such property in trust for purposes named.* 26 R. C. L. 1182. *And any words which indicate with sufficient certainty a purpose to create a trust will be effective in so doing. Gutch v. Fosdick,* 48 N. J. Eq. 353, 22 A. 590, 27 Am. St. Rep. 473; *Faulds v. Dillon,* 231 Mich. 509, 204 N. W. 733. While the petitioner here may be said to have had control of the money which it had placed in the maintenance fund, diversion of that fund for corporation purposes or any purpose other than that designated by its promise to maintain the same, and the specific resolution of its board of directors to devote to that purpose 20 per centum of its receipts from sales, might be enjoined by a suit in equity as a violation of the trust agreement. The crucial question is, Did the petitioner's patrons possess the right to protect themselves and demand the preservation of the fund which the petitioner had covenanted with them to maintain and by its resolution had set apart for maintenance? That question is by the authorities answered in the affirmative. 26 R. C. L. 1359; *Rodney v. Shankland,* 1 Del.

Ch. 35, 12 Am. Dec. 70; *Linneman v. Moross,* 98 Mich. 178, 57 N. W. 103, 39 Am. St. Rep. 528."

In 26 R. C. L. 1182 therein cited the well settled rule is stated as follows:

> "*The owner and donor of personal property may create a perfect or complete trust, by his unequivocal declaration in writing, or by parol, that he himself holds such property in trust for the purposes named.* The crucial question where a voluntary trust in the settlor is sought to be established is whether the declaration on which such trust is sought to be predicated is sufficient. *There is no prescribed form for the declaration of a trust; whatever evinces the intention of the party that the property of which he is the legal owner shall beneficially be another's is sufficient.*"

In *Chicago, etc., Ry. Co. v. Des Moines, etc., Ry Co.,* 254 U. S. 196, 65 L. Ed. 219, 41 S. Ct. 81, supra, the court said:

> "It needs no particular form of words to create a trust, so there be reasonable certainty as to the property, the objects, and the beneficiaries. *Colton v. Colton,* 127 U. S. 300, 310, 32 L. Ed. 138, 142, 8 Sup. Ct. Rep. 1164. . . . But it is not necessary that the trust be expressed in the same instrument that transfers the title. Various instruments may be read together in order to ascertain the intention to establish one. *Loring v. Palmer,* 118 U. S. 321, 340, 30 L. Ed. 211, 218, 6 Sup. Ct. Rep. 1073."

Also directly in point is the tax case of *O'Meara v. Commissioner of Internal Revenue,* (C. C. A. 10) 34 F. 2d 390. There the taxpayers transferred a certain oil lease to a corporation. Construing together the different instruments involved in the transaction, it appeared that the grantors reserved to themselves the equitable beneficial title, al-

though conveying the legal title to the corporation. The court held that this established a trust and was not a sale, as there was no transfer of the beneficial or equitable title even though there was a conveyance of the legal title, and consequently the transaction was not taxable. The court said:

> "The declaration of trust need not be contained in the instrument which transfers the legal title. It may be set forth in a separate instrument or in several instruments, provided they are related to and connected with each other and, when construed together, establish the existence of the trust. (Citing cases). Therefore, as between the parties and the corporation, the proposal, the resolution of acceptance, the assignments and the certificate of stock constituted one transaction and the intent of the parties must be gathered from an examination of all of these instruments. We conclude that these instruments, considered together, manifest an intention to transfer to the corporation the legal title to the leases and personal property used in connection therewith, as a managing trustee, and to retain the equitable title to such property in the assignors. . . .
>
> "It is our conclusion that the deficiencies should be set aside in so far as they were based upon the transfer of the oil and gas leases to the Orlando Company."

In *Foreman v. Foreman,* 251 N. Y. 237, 167 N. E. 428, Judge Cardozo speaking for the court said:

> "The rule is now settled by repeated judgments of this court that the statute does not obstruct the recognition of a constructive trust affecting an interest in land where a confidenial relation would be abused if there were repudiation, without redress, of a trust orally declared. (Citing cases). . . .

"The wife, far from attempting to rid herself of the trust because orally declared, submitted to it as completely as if seals and parchments had perfected the evidence of duty. Cf. *Bork v. Martin,* 132 N. Y. 280, 30 N. E. 584, 28 Am. St. Rep. 570. No objection was heard from her, or none that has been disclosed, when the husband gathered in the rents and used them for himself. *In its origin the trust was dependent for proof of its existence on nothing better than word of mouth. In the end, at her death, what was oral in its beginnings had been confirmed by part performance, with the result that conduct as well as words had become the signs of its creation. Jeremiah v. Pitcher,* 26 App. Div. 402, 49 N. Y. 788, affirmed 163 N. Y. 574, 57 N. E. 1113; *McKinley v. Hessen,* 202 N. Y. 24, 95 N. E. 32; *Burns v. McCormick,* 233 N. Y. 230, 135 N. E. 273. The wife would have been guilty of an abuse of confidence by disclaimer during life. Her heir will not be suffered to nullify her submission to the call of equity and honor by disclaimer after death. . . .

"It is reinforced by words of promise, by the relation of man and wife, and by unequivocal acts of confirmation and performance. In such circumstances, the plastic remedies of the chancery are moulded to the needs of justice. . . . What has been written assumes that the testimony of the plaintiff's witnesses is truthful and accurate. As to this there is a question of credibility which the trier of the facts, and not this court, must resolve."

Bearing in mind the rule of *Erie Ry. Co. v. Tompkins, supra,* in Washington, where these transactions occurred, these rules are fully recognized.

In *Tucker v. Brown,* 199 Wash. 320, 92 P. 2d 221, the court held that a trust existed as to a large amount of valuable property, although there was nothing whatever in writing signed by the alleged trustee, and there was no

testimony available from any party to the transaction, both of them being then deceased. The court said:

> *"An express trust is one created by the act of the parties; and, where a person has, or accepts, possession of money, promissory notes, or other personal property with the express or implied understanding that he is not to hold it as his own absolute property, but to hold and apply it for certain specified purposes, an express trust exists. Farrell v. Mentzer,* 102 Wash. 629, 174 Pac. 482; 65 C. J. 295; *Allen v. Hendrick,* 104 Ore. 202, 206 Pac. 733.
>
> *'A person occupying a fiduciary relation, who has property deposited with him on the strength of such relation, is to be dealt with as trustee of an express trust. Moulden v. Train,* 199 Mo. App. 509, 204 S. W. 65."

In *Holmes v. Holmes,* 65 Wash. 572, 118 Pac. 733, the court said:

> "The important and decisive question in the case is, can an express trust be proven by a writing signed by the trustee. We think the question must receive an affirmative answer. . . .
>
> "In *Barrell v. Joy,* 16 Mass. 220, it is said: 'But it seems to be settled, by authorities cited at the bar, that any declaration in writing, made by the grantee or assignee of property, at any time after the conveyance, is competent proof that the property was to be holden in trust according to the terms of such declaration, within a fair and liberal construction of the statute of frauds; and that *letters or other papers, however informal, are sufficient to constitute such declaration.*' "